OWNERSHIP ORGANIZATION AND FIRM PERFORMANCE

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ABSTRACT

This essay reviews research on the type and degree of fragmentation of firm ownership with an emphasis on the consequences of ownership organization for firm performance. We use a property rights approach to synthesize sociological, organizational, legal, and economic research that has examined the effect of ownership organization on firm performance. Agency theorists generally assume that shareholders are homogenous and that their influence on firm performance is directly proportional to the percentage of equity they hold. However, empirical research following this approach has failed to produce definitive evidence. Class analysis perspectives interpret these inconclusive results as demonstrating that, regardless of ownership organization, firms are run to serve the capitalist class. An alternative interpretation is that shareholders are not homogeneous but that certain types of shareholders use their formal authority, social influence, and expertise to "capture" property rights and strongly influence firm performance. The influence of different types of owners may depend on industry characteristics, and we review literature pointing to a contingency theory of ownership organization.

INTRODUCTION

Recent work in organizational sociology has made considerable progress toward understanding how certain features of the governance systems found in modern public corporations affect a range of important firm outcomes. The functional backgrounds of corporate officers, the proportion of outsider directors, the separation of the Chairman and CEO positions, and the social net-
works found across firms have been used to predict outcomes such as poison
pill adoption, corporate diversification policies, and the use of the multidivi-
sional organizational form. This research has generally downplayed the role of
ownership in corporate governance and assumed that ownership and control
are effectively separated. By contrast, financial economic research continues
to question the role of ownership in understanding control of the firm, although
this research tradition has produced highly mixed results on the relationship
between ownership organization and performance.

The study of ownership organization and its effect on performance should
not be left completely to financial economic research. The study of who con-
trols the use of capital and how this control affects the creation and distribution
of wealth in society has long been an important line of intellectual inquiry,
originating with Marx. Studying the relationships of individuals and firms to
property with a broader and more flexible approach may provide important
insights into the efficiency and distributive consequences of modern capitalist
firms, or so we hope to show. The actual and potential contributions of sociol-
ogy to this line of inquiry seem particularly important at the present time, and it
is therefore timely to assess what is known, and not known, about the effects of
ownership organization on firm performance. We propose an approach based
on “ownership type” that views ownership as a key organizational variable in
determining firm outcomes.

In the sociological and economic literature on organizations, the modern
firm is usually seen as a large organization with four main groups of actors:
shareholders, boards of directors, top executives and other managers, and
workers. Shareholders are thought of as “owners”; they provide financial capi-
tal and in return receive a contractual promise of economic returns from the
operations of the firm. Directors act as fiduciaries of the corporation who may
approve certain strategy and investment decisions but whose main responsibil-
ity is to hire and fire top managers. Managers operate the firms; they make
most business decisions and employ and supervise workers. Workers carry out
the activities that create the firm’s output.

This image of the modern firm accurately reflects the organization of many
large public corporations that dominate the US economy. However, many
other firms are organized in ways that merge two or more of these tasks: Own-
ers may be both investing and managing, workers may be owners, managers
may acquire large shares of ownership, and so forth. In entrepreneurial firms,
one person fuses all four tasks: investing, monitoring, managing, and working.
In fact, owner-managed firms were the origin of capitalist production and
dominated the US economy until the twentieth century. However, as firms in
industries such as steel, railroads, and oil expanded their operations, individual
and family owners found that they did not have enough wealth to finance
large-scale industrial operations (Chandler 1977). Firms began the practice of
issuing shares to raise the large amounts of capital necessary for growth and
geographic expansion. As a result, many firms, particularly large firms, are no
longer owner-managed firms but corporations, sometimes with thousands of
shareholders each of whom owns only a small fraction of the shares.

The fragmentation of the owner-managed firm and its consequences have
interested sociologists, legal scholars, and economists for a very long time.
Karl Marx discussed the fragmentation in Volume III of Capital, characterizing
the resulting separation as "the abolition of capital as private property within
the framework of capitalist production itself" (1867). The consequence of this
fragmentation for the class structure has generated a debate among sociolo-
gists, to which we return below. However, the main impetus to studying the con-
sequences of the fragmentation of the owner-managed firm in organizational
sociology and economics was Berle & Means' The Modern Corporation and
Private Property (1932). Berle & Means document the "separation of owner-
ship and control" and depict the corporation as a largely autonomous entity,
where executives and managers successfully pursue their own objectives of
growth and stability rather than maximizing the returns to the shareholders. A
large literature in organizational sociology and economics adopts this "mana-
gerialist" perspective which assumes autonomous managers control firms.

OWNERSHIP ORGANIZATION AND FIRM
PERFORMANCE: AN OVERVIEW

In this essay, we review research and scholarship on the organization of own-
ership resulting from the fragmentation of the original owner-managed firm
and the consequences of these ownership patterns, especially for firm perform-
ance. Our perspective differs from the conventional separation of ownership
and control conception. The contrast between the large autonomous and
management-controlled corporation and the owner-managed firm is an over-
simplification. There are more than two types of ownership organization.
Modern firms have a variety of ownership patterns, and exploring ownership
type recognizes that large-block shareholders are not homogenous and that
certain types of owners have a disproportionately large impact on corporate
governance. Some very large firms are dominated by large-block shareholders
who have a seat on the board of directors, some by shareholders who sustain
their ownership blocks over time, and some by families owning large bocks of
shares. Recent research has shown, using accounting and stock price-based
measures, that each of these ownership types is associated with enhanced
performance (Kang 1998a).

Additional ownership types include top executives, employee stock owner-
ship plans, buyers, suppliers, different types of institutional investors, lever-
aged buyouts, and venture capital. Top executive stock ownership has recently
received considerable attention, as there is currently a trend toward compensating executives with stock options. However, little compelling evidence exists of the effects of these developments on firm performance (Loderer & Martin 1997, Bhagat & Black 1998). Employee stock ownership has been found to have some positive effects on profitability, productivity, and compensation (Blasi et al 1996). Although buyers and suppliers have been identified as having potentially important relationships through cross Holdings of equity, only anecdotal evidence suggests that these owners affect performance (Porter 1992).

Another important ownership type is institutional investors, such as public pension funds and private mutual funds, which now hold approximately 60% of all outstanding US equities. A small number of these investors, usually public pension funds such as CalPERs, have recently become more active in corporate governance, largely through the use of media condemnation or "jawboning" to influence managers. Research on the effect of this shareholder activism or "relational investing" on firm performance has produced mixed results (Bethel et al 1998, Bhagat et al 1997). These investors typically do not conduct proxy fights and do not try to elect members to the board of directors. Research has failed to produce strong evidence on a correlation between the percentage of shares owned by institutions and firm performance (Chaganti & Damanpour 1991, Black 1998). Finally, anecdotal evidence suggests that specialized investment funds run by skilled managers who purchase large blocks of shares may in some cases improve the firm performance (Pound 1992).

Firms may fundamentally change their ownership patterns over time. A particularly interesting and controversial example of changing ownership patterns can be found in the recent wave of buyouts, called leveraged buy-outs (LBOs), of large public corporations by investment groups, which use enormous amounts of debt to transform public corporations into private, owner-dominated firms. The value of LBOs and their resulting changes in ownership patterns have been widely debated, as some researchers have presented evidence that the reorganization of ownership patterns improved the efficiency of the firm, while others argue these gains occurred at the expense of workers and communities (Jensen 1989, Kaplan 1991, Shleifer & Summers 1988). Another interesting example of changing ownership forms are the many entrepreneurial firms that begin as private firms that rely on venture capitalists at founding, but then within a few years use initial public offerings to place a significant portion of equity in the hands of public shareholders. Research on venture capital suggests that this form of concentrated ownership may lead to increased performance, although there is now evidence that firms may continue to perform well even after venture capitalists have sold their equity stakes (Sahlman 1990, Black & Gilson 1998, Mikkelson et al 1997).

Our review integrates sociological literature on ownership with approaches from managerial economics that use a principal-agent perspective on the rela-
tionship between the various groups of actors in the modern corporation. We first survey ideas about property rights that present a framework for analysis of ownership organization and its consequences. We then present the principal-agent conception of the firm that has inspired much of the research on the consequences of ownership fragmentation, and we examine the empirical evidence on the relationship between ownership concentration and performance. A review of the debate on the consequences of ownership fragmentation for the class structure follows. We then review organizational approaches to the analysis of the relationship between ownership organization and firm governance and suggest a synthesis of theory in understanding ownership and performance that sees the “fit” between certain ownership types and the industry context as shaping firm performance.

PROPERTY AND THE LEGAL RIGHTS OF SHAREHOLDERS

Our basic thesis is that the organization of ownership matters for firm performance because the organization of ownership allocates property rights, or control of assets, to various actors involved in a firm—in the owner-managed firm to a single actor, in the typical corporation to many actors. These property rights present opportunities for actors to realize their interests and affect firm performance. For example, family owners of large blocks of shares may force firms to remain in less profitable geographical locations. Or, managers may use their control of operational decisions to divert firms into unprofitable endeavors that may benefit managers’ careers but decrease the return to shareholders.

Property rights here are conceived of broadly as the rights to the benefits, use of, and disposal of goods and assets. The metaphor of property as a “bundle of rights” is useful in conceptualizing how organizational actors are able to influence organizational outcomes (Hohfeld 1913). As noted by Corbin, “Our concept of property has shifted, incorporeal rights have become property. And, finally, ‘property’ has ceased to describe any res, or object of sense, at all, and has become merely a bundle of legal relations—rights, powers, privileges, immunities” (1922:429). In the classic “atom of property” (Berle & Means 1932), the benefit, use, and disposal rights are fused. In the conception of the classic owner-managed firm, the same individual receives the benefits from the asset she controls, decides completely about its uses, and can dispose of the property fully. The separation of ownership and control in the modern corporation described by Berle & Means is a particular fragmentation of these rights, where benefit rights and use rights have been separated.

The fusion of all rights in the “atom of property” is the exception rather than the rule. Even in ordinary market transactions, rights are often not completely
fused. With goods sold with warranties, the seller retains some of the use rights by making the warranty dependent on meeting certain obligations—regular oil changes for cars, for example. Prospective buyers can gain some of the benefit rights, as when customers pick and choose the best cherries in a batch without the owner being easily able to prevent it (Barzel 1997).

Rights become fragmented in two main ways. First, they may be simply assumed or captured because the original holder of the right cannot protect the right because the costs are too high. It may be too costly to ascertain the properties of the good or asset, such as in the cherry-picking example. Or, free-rider problems may make it too costly for an individual to monitor the asset, such as when executives use cash flow to acquire corporate jets. Second, rights become fragmented because they are delegated by contracts. Contracts are sometimes explicit or complete contracts, as in the warranty example. However, contracts are often incomplete because of the high transaction costs of negotiating every possible future contingency, and they are therefore subject to further fragmentation due to capture. For example, employment contracts are usually incomplete contracts, where the delegation of use rights to employees is done by the original owners, who retain control over benefit rights. These benefit rights are subject to capture as employees use bargaining powers derived from firm specific skills or collective actions to capture rents (Sorensen 1996).

Rights and contracts transferring or delegating rights may be enforced by the state, making them legal rights. However many rights are captured or transferred without legal support as when managers control cash flows to live more glamorously. Legal rights may be seen as one of several possible means to obtain what Barzel (1997) calls economic property rights, which are what people ultimately seek. Economic rights can be defined, following Barzel (1997:3), as the ability to consume some good, or the services of an asset, directly, or to consume it indirectly through exchange. These rights are not constant; they are dependent on the efforts of protection, the capture attempts by others, and governmental protection through police and the courts.

Legal rights are important because they protect economic rights and define the basic context for the exercise and transfer of rights. In particular, legal rules are the foundation of modern corporate governance, as the property rights of shareholders are created and defined by federal securities regulations and case law. Shareholders may be viewed as parties that have explicitly contracted for a relatively well-defined subset of rights as prescribed under the corporate charter. A close examination of the formal legal rights assigned shareholders reveals three key rights:

1. The right to share pro rata (that is, the same amount for each share) in dividend payments, if and when the directors exercise their discretion to declare dividends, and to share pro rata in distributions in liquidation of the enter-
prize. 2. The right to vote, on a one share—one vote basis, upon the election of directors and certain major corporate changes such as mergers with other companies and liquidations. 3. A restricted but not negligible right to information in the form of a shareholder’s right to inspect corporate books and records. (Clark 1986:13)

Shareholders in public corporations have very limited rights compared to the “owners” found in other legal forms of organizing such as partnerships. Under the legal doctrine of limited liability, shareholders of public corporations do not bear the risk of facing legal claims against their personal assets. By contrast, partners not only risk their initial investment, but they also are personally liable for legal claims brought against the partnership. Therefore, shareholders’ legal powers within the corporation should be viewed as highly limited in scope and very different from the broad legal powers given to “owners” of other organizational forms or other types of assets.

The legal limits in shareholder power are important in understanding control of the corporation because shareholders seldom have physical control over the complex assets of the corporation. Property law initially defined ownership in terms of the physical possession of assets (Berle & Means 1932). As Oliver Wendall Holmes discusses in *The Common Law*, “But what are the rights of ownership? They are substantially the same as those incident to possession. Within the limits prescribed by policy, the owner is allowed to exercise his natural powers over the subject-matter uninterfered with, and is more or less protected in excluding other people from such interference. The owner is allowed to exclude all, and is accountable to no one but him” (1881:246). However, in the modern corporation it is not the shareholders, but rather the managers and workers, who come closest to physically “possessing” the firm’s assets. These assets are often complex, such as in the case of large-scale production facilities and research laboratories. Most shareholders cannot determine whether these assets are being used correctly, lacking both the information and expertise needed to monitor the activities that take place.

Most shareholders only own a small fraction of the total number of shares and face considerable costs in conducting effective monitoring. Although shareholders have legal rights to benefits from corporate assets, these benefit rights may routinely be captured by other organizational participants, including board members, managers, workers, or other shareholders. The central issue that occupies our review is the inability of shareholders with their limited use rights to capture many of these benefit rights.

The existence of rights and the potential for obtaining or capturing benefit rights provide incentives that are opportunities for actors to increase their wealth. They act on these opportunities according to the formal authority, social influence, and expertise that govern their behavior. Therefore, this broad conception of property rights allows for the integration of economic ideas that
feature a narrow conception of contracts and exchanges with sociological ideas about the social processes and structures that shape people's responses to incentives and the opportunities they present. Ownership is a complex economic and sociological phenomenon occurring in a legal context that creates incentives and opportunities to capture property rights and take actions that shape firm performance.

AGENCY THEORY AND THE THEORY OF THE FIRM

The property rights perspective directly informs the rich literatures on the firm found in legal theory and organizational economics, where the distinction between the market and the firm for organizing transactions has been a major concern. The idea that property rights rarely are absolute and that benefit, use, and disposal rights often are fragmented explains why firms often incur agency costs (Jensen & Meckling 1976) and transaction costs (Williamson 1985). These are the costs associated with transfer, capture, and protection of rights (Barzel 1997:4). In particular, the view that principals delegate rights to agents and are therefore faced with the problem of alignment of the agents' interests in order to maximize firm performance has generated an important literature in managerial economics.

An agency relation is one where a "principal" delegates authority to an "agent" to perform some service for the principal. These relations may occur in a variety of social contexts involving the delegation of authority, including clients and service providers such as lawyers, citizens and politicians, political party members and party leaders, rulers and state officials, employers and employees, and stockholders and managers of corporations (Kiser 1998). Sociologists have recently used ideas regarding principal-agent relations to explore a wide range of social phenomena (Kiser 1998). Sociological research using agency theory approaches includes Adams' (1996) discussion of agency problems involved in colonial control, Kiser's (Kiser & Tong 1992, Kiser & Schneider 1994, Kiser 1994) work on the organizational structure of early modern tax administration, Gorski's (1993) analysis of the "disciplinary revolution" in Holland and Prussia, and Hamilton & Biggart's (1980, 1984, 1985) arguments about control in state government bureaucracies. Similarly, current work in political science has also used agency theory approaches to explore state policy implementation (Weingast & Moran 1983, Bendor & Moe 1985, Wood 1988, Kiewiet & McCubbins 1991).

Applied in the corporate governance context, agency theory recognizes how fragmented property rights may significantly affect firm performance. Agency theorists conceptualize the firm as a "nexus of contracts" where rights are delegated to the various groups of actors (Jensen & Meckling 1976). This contractual view provides an elegant formal conception of the firm, where all
contracts can be treated as formally alike. Firms perform well when the system of contracts offers an efficient alternative to other organizational forms and to markets. Firms that survive minimize agency costs and provide the quality of the product or service demanded at the lowest price, while covering the full costs of production. Maximizing claims for shareholders is thought to be consistent with these efficiency criteria (Fama & Jensen 1983). The aspect of the organization of ownership emphasized in this literature is the alignment of the parties' interests through the use of contracts, in particular using contracts to align the interests of managers with the interests of shareholders.

Agency theorists suggest that the separation of ownership and control is often the best available organizational design, as the benefits of increased access to capital and professional management typically outweigh the costs associated with delegating control of business decisions to managers (Fama & Jensen 1983). However, in the absence of strong corporate governance systems, public corporations may suffer in performance when self-interested managers pursue their own interests rather than the interests of shareholders (Jensen 1989). Managers have opportunities for pursuing their own interests—in prestige, luxurious accommodations and modes of transportation, and high salaries—because they have been delegated rights through their contracts to control cash flows and information in their firms. Modern public corporations often are faced with considerable agency costs. It is expensive to gather information and assess managerial actions, and particular shareholders only gain a fraction of any pecuniary benefits produced, proportional to the percentage of total equity they own (Shleifer & Vishny 1989). This creates collective action problems. Gains are available to all shareholders regardless of whether they have incurred the costs of monitoring, a problem that contributes to the separation of ownership and control (Berle & Means 1932). Because the costs of participating in corporate governance typically exceed the benefits, and because of the problem of free riding, dispersed shareholders are generally unlikely to participate in corporate governance.

Large-block shareholders potentially have an important role in reducing agency costs in public corporations. Because large-block owners must obtain sufficient returns to make their participation in corporate governance cost-effective, public corporations with concentrated owners are thought to enjoy lower agency costs, resulting in superior performance relative to corporations with fragmented ownership (Fama & Jensen 1983, Jensen 1989, 1993). One way to align the interests of shareholders and managers is for firms to raise a large portion of the capital they require by issuing debt rather than equity. Debt covenants require periodic debt repayments, forcing managers to generate cash and pay it out rather than use it to invest in new projects or perquisites. The heavy use of debt financing also enables individual shareholders to own a larger proportion of the firm's total equity for a given amount of capital in-
vested, as the total value of the equity outstanding is considerably smaller in highly leveraged firms. As a result, the large-block shareholders found in LBOs have substantial voting rights in corporate governance and the financial incentive to monitor closely the activities of the firm. Agency theorists argue that these changes in ownership, combined with changes in top management teams, improve the efficiency of firms (Jensen 1989). Agency theory provides an elegant argument for how ownership organization affects firm performance. We consider next the empirical evidence on the link between organization and performance that bears on this argument.

CONCENTRATED OWNERSHIP, CONTROL, AND FIRM PERFORMANCE

Considerable empirical research explores the link between concentration of ownership and performance from both economic and sociological perspectives. Large-sample financial economic studies measuring the effect of concentrated ownership on performance in public corporations find mixed results when examining the overall concentration of ownership and the percentage of shares held by insiders or institutional investors (Demsetz & Lehn 1985, Holderness & Sheehan 1988, Zeckhauser & Pound 1990, Cho 1998, Black 1998). For example, in their study of 511 large US public corporations, Demsetz & Lehn (1985) suggest that concentrated ownership rises to its appropriate level for each industrial context such that it has no measurable effect on performance, a conclusion we shall return to later.

Many studies have simply dichotomized ownership concentration by characterizing firms as manager-controlled or owner-controlled. Managerial control is inferred when the concentration of ownership is low so that the largest shareholder holds between four or five percent (Salancik & Pfeffer 1980, Berle & Means 1932) to as high as 20% (Burch 1972). A study that distinguished among owner-controlled, manager-controlled, and owner-managed firms found that owner-controlled and owner-managed firms produced significantly higher rates of return on investment than did manager-controlled firms (McEachern 1975). However, most studies using ownership thresholds indicate little or no difference, either in profit margin rate or rate of return to stockholders, or between owner-controlled and manager-controlled firms (Kamerschen 1968, Monsen et al 1968, Lewellen 1969, Larner 1970, Hindley 1970, J Palmer 1973). This large literature using ownership thresholds has been reviewed by Scherer (1988).

The mixed results on the relationship between ownership concentration and performance can be given one of three possible interpretations. One interpretation is that the Berle & Means thesis about the separation of ownership and control is an empirical "pseudofact," where existing empirical measures of
“control” do not sufficiently account for the complex social context in which ownership occurs. Zeitlin argues that modern public corporations, whether appearing outwardly to be run by managers, owner-managers, or large shareholders, are ultimately governed in the interest of the capitalist class in the manner conceived of by Marxist scholarship (1974). We address this perspective in greater detail below.

A second interpretation is that surviving firms enjoy the level of ownership concentration that is most efficient for their industrial and institutional environment. This is the interpretation suggested by Demsetz & Lehn (1985), Kole (1994) and Cho (1998). Ownership organization is considered endogenous and not an independent influence on performance. However, this approach assumes that ownership structures are in equilibrium and does not address the possibility that longitudinal evidence on ownership and performance may reveal that certain ownership structures are generally associated with increased firm performance. Other evidence also suggests that the matter is more complicated. For example, research that distinguishes among different types of large-block institutional investors finds that large mutual funds, foundations, and pension funds are more likely to affect organizational decision-making than other large-block shareholders (Brickley et al. 1988). We review below other research that suggests that the characteristics of large-block owners matter for performance.

A third interpretation of the mixed empirical evidence found regarding the effects of ownership concentration on firm performance is that examining formal ownership rights does not adequately capture important social dimensions of ownership. Agency theory’s view of the firm as a nexus of contracts where property rights are precisely meted out by contracts may not sufficiently explain firm outcomes (Demsetz & Lehn 1985, Morck et al. 1988). Focusing on the delegation of the formal rights of shareholders is conceptually appealing because it helps avoid the problem of reification, where the corporation is thought of as a single entity and the legal rights arising from corporate assets are thought of as indivisible. However, simply defining property rights in corporate assets in terms of principal-agent relationships or formal, contractual rights may overlook interesting and important questions regarding who “captures” these property rights and how this affects firm performance. The theory and evidence for this interpretation is considered below, after we consider the class analysis perspective.

CLASS ANALYSIS, OWNERSHIP, AND PROFIT

Marx proposed a model for capitalist production that saw capitalists forced by competition to act to maximize profits and the rate of exploitation, resulting in maximum firm performance. In general, this analysis pays little attention to
the particular characteristics of capitalists and the manner in which ownership is organized. However, as previously noted, Marx did present a brief discussion of joint stock companies and saw them as the “abolition of capital as private property.” This statement has been given two very different interpretations. One interpretation, first proposed by Dahrendorf (1959), is consistent with the Berle & Means’ (1932) fragmentation of ownership tradition and agency theory. The second interpretation, suggested by Zeitlin (1974), argues that the “abolition of capital” should be understood as a transformation of capital rather than an elimination of capital.

Dahrendorf argues that Marx understood the “socialization of ownership” as weakening capitalism by reducing the incentives of capitalists to maximize performance, thus resulting in a fundamental change in capitalist society and the transformation of capitalism from within into “industrial society” (Dahrendorf 1959). In particular, managers will be less likely than owners to maximize the efforts of workers. As a result, firm performance is likely to decline, with the distributive consequence that wealth is transferred from shareholders to workers. Dahrendorf suggested that professional managers are not simply the capitalist oppressors of workers, but rather that “Capital—and therefore capitalism—has dissolved and given way in the economic sphere” to independent conflict fronts, where the subjected classes of industry and of political society are no longer identical, as opposed to the politically and economically oppressed worker class described by Marx (Dahrendorf 1959:47).

Similarly, work by Wright suggests that modern capitalism has resulted in a situation where managers occupy “contradictory” locations because “they share class interests with two different classes but have interests identical to neither” (1980:331). If the firm performs well, the managers’ value on the market for managerial talent will increase somewhat. However, because they often work closely with workers, managers may feel closer social ties with workers, and they may be willing to transfer the shareholders’ money to workers rather than to extract the maximum amount of labor possible from them (Shleifer & Summers 1988).

Zeitlin interprets Marx as seeing a transformation into a new, but still capitalist, capitalism. Corporations may appear outwardly to be controlled by managers, but capitalists such as large-block family owners and their “kinship” groups may actually control these firms, causing managers to work in the interests of the “proprietary interests” of the capitalist class (Zeitlin 1974). Zeitlin argues that as an empirical matter, the separation of ownership and control has been greatly exaggerated and suggests large-block owners actually controlled many of the public corporations originally studied by Berle & Means. These large-block owners were often families, where founders had passed down “control” of the corporation through the transfer of significant, though not majority, ownership stakes to their heirs (Zeitlin et al 1975). In
any event, it does not much matter for performance who controls the firms, as all the main actors are believed to work in the interest of the capitalist class. Zeitlin criticizes empirical work on ownership and performance and suggests that the concept of "control" requires a more context-specific understanding.

Other research in this tradition suggests that managers are a group of networked elites that use interlocked boards of directors to pursue their own interests as well as promoting the general interests of large business (Useem 1980). Domhoff suggests that "The growth and interconnections of corporations... have meant the rise of a more sophisticated executive elite which now possesses a certain autonomy from any specific property interest. It's the power of property, but that property is not always or even usually of one coherent and narrow type. It is, in operating fact, class-wide property" (1967:40).

The argument that firms are run in the interest of the capitalist class, regardless of ownership organization, raises the question of how the capitalist class exercises its influence. This question has produced a large literature in sociology and political science, reviewed, for example, by Glasberg & Schwartz (1983), on who controls the large corporations: large-block shareholders including families, banks, or the managers themselves. Control has been defined in terms of the power to determine the broad policies guiding the corporation, including decisions regarding capital structure, product diversification, corporate structure, and mergers (Herman 1981, Fligstein & Brantley 1992). However, much of the organizational literature on interlocks pays considerable attention to identifying patterns of interlocking directorships and much less attention to what control means for the performance of firms (Useem 1980, Palmer 1983).

The class analysis perspective suggests either that Marx had foreseen the Berle & Means thesis and a fundamental transformation of capitalist society, or that he had envisioned the continuation of capitalism with new key actors such as elite managers and banks acting in the interests of the capitalist class. Research using the latter perspective suggests that although managers may not always have their interests aligned with the particular shareholders that are their principals, their interests may be aligned with the capitalist class as a whole. Neither interpretation has produced evidence on variation in firm performance by ownership organization.

Class approaches to the topic of ownership organization and performance have raised important questions regarding the distributive consequences of the ownership patterns found in modern corporations. As Dahrendorf notes, "class is always a category for purposes of the analysis of the dynamics of social conflict and its structural roots, and as such it has to be separated strictly from stratum as a category for describing hierarchical systems at a given point in time" (1959:76). Zeitlin argues that understanding families as "kinship units" that
perpetuate class relations is one useful approach (1974). Yet, surprisingly little sociological research has attempted to understand how the evolution of ownership organization has affected modern class relations. Recent economic research on ownership distribution in US society has found that increasing institutional ownership has increased the disparity in income distribution in the US population (Poterba & Samwick 1995). The question of who gains from superior performance in corporations—who enjoys the benefit rights to corporate profit—appears worthy of more extensive sociological inquiry, as the efficiency and distributive consequences of economic activity are highly intertwined and have together shaped the legal rules surrounding corporate governance (Bromley 1989, Roe 1991, 1994).

ORGANIZATIONAL STUDIES AND OWNERSHIP TYPE

Most research in the sociology of organizations fundamentally assumes that managers control the modern public corporation. This approach, known as "managerialism," assumes that most of the use rights and benefit rights that arise from corporate property have already been captured by managers, and that the most important areas for inquiry are those that investigate social influences on managers. Because managerialism is assumed, most organizational research on "corporate governance" has focused on variables other than ownership. At the same time, this organizational research has deemphasized the question of organizational performance, instead focusing primarily on other organizational outcomes. For example, managers have been characterized as having "conceptions of control" where their actions regarding strategic decisions are seen as being greatly shaped by institutional factors that affect a very broad range of dependent variables, primarily focused on firm strategy (Fligstein 1990, Fligstein & Brantley 1992). Other organizational research has explored how networks of intercorporate relations affect the adoption of organizational practices such as poison pills and golden parachutes (Davis 1991, Davis & Greve 1997), the payment of acquisition premiums (Haunschild 1993), financing, and capital structure (Mizruchi & Stearns 1994), and intercorporate coordination (Palmer et al 1986). Additional organizational research on corporate governance has focused on board characteristics and how they affect the payment of greenmail (Kosnik 1987), CEO turnover (Ocasio 1994), and diversification strategy (Westphal & Zajac 1997). Research that has surveyed the effects of board composition has found an uncertain relationship between board composition and firm performance (Bhagat & Black 1998). Organizational research on corporate governance finds that managers engage in "symbolic action" by announcing, but not actually implementing, actions that engender positive stock market reactions (Westphal & Zajac 1998). Although organizational research has explored many important aspects of corpo-
rate governance, this research typically uses concentration of ownership simply as a control variable, having very little to say on how ownership patterns affect organizational performance.

Taking "managerialism" for granted and concentrating on how resource dependency and institutional forces affect managers does not sufficiently recognize informal and formal empirical evidence that certain types of large-block shareholders exercise influence in corporate governance using formal authority and informal power. Agency theory's emphasis on the importance of ownership concentration offers an important starting point in understanding ownership organization. As argued above, the mixed evidence for the link between ownership concentration and performance may reflect that in agency theory, ownership is seen as a purely economic variable, where owners are homogenous and the influence of ownership is a function of ownership concentration. Owners with comparably sized ownership stakes may vary considerably in their capacity to influence managers and the firm because concentrated ownership limits managers' potential alternative sources of support for their decisions (Salancik & Pfeffer 1980). Different types of shareholders have different sets of benefit rights and use rights, and their willingness and ability to monitor managers may vary according to the amount of contractual and non-contractual benefit rights and use rights they possess. Although shareholders may sometimes have complex goals, increasing their benefits by increasing the economic value of their large-block ownership stake is very likely to be their primary goal. At the same time, some benefits outside of stock price appreciation may be important. This may be critical for some ownership types, such as family large-block owners. Not only may shareholders differ in their objectives, they may also differ in how likely it is that they can realize their objectives. In particular, large-block owners have three potential bases of power that they may leverage to influence firm outcomes: formal authority, social influence, and expertise.

Three Bases of Shareholder Power

All shareholders have some power based on their legal rights, or formal authority (Weber 1968). These powers include the right to vote on ratification of nominations to the board of directors and the right to approve some major business decisions such as mergers and acquisitions (Clark 1986). If shareholders are of sufficient size to overcome free rider problems, they may obtain active roles in the governance structure of the firm, such as a seat on the board of directors, which provide them with additional formal authority and direct involvement in key strategic decisions. When ownership is coupled to a "strategic position" such as a high executive office or a directorship, it enables their possessors to participate in making key decisions (Herman 1981). Although
directors are frequently criticized for being passive "pawns" of management, outside-director shareholders are more likely to be "potentates" (Lorsch & MacIver 1989) who overcome the problems of passive, dysfunctional boards. Several financial economic studies have found a nonmonotonic relationship between the magnitude of insider stock ownership and firm performance (Morck et al 1988, McConnell & Servaes 1990, Cho 1998). For example, Morck et al find that insider ownership between 0 and 5% increases firm performance, insider ownership between 5% and 25% decreases performance, but that insider ownership above 25% again increases performance (1988).

Second, shareholders also have power based on social influence that they develop through interactions that occur in the context of formal organizational roles, through repeated interactions between owners and managers over time, and through rich histories of relationships that may develop between owners and workers over several generations. Consistent with this view, large-block shareholders who maintain their ownership stakes increase their social influence over time. Social influence is an important base of power, as interpersonal relations significantly shape important resource allocation decisions in organizations (Pfeffer 1992). Social influence is important in corporate governance as suggested by the finding that CEOs able to appoint more outsiders to their board are more likely to have golden parachutes (Wade et al 1990). General evidence on the importance of social influence is provided by research that has focused on demographic backgrounds of participants as a source of political power (Zajac & Westphal 1995, 1996).

Third, certain types of large-block shareholders may have power based on their expertise. Expertise is a superior understanding of the firm and its industry and general business skills that can be used in managing critical environmental dependencies (French & Raven 1968, Pfeffer & Salancik 1978, Finkelstein 1992). This expertise is often acquired through participation in the firm’s governance structure, such as serving on the board of directors, observing and participating in important strategic decisions over time, and in managing the firm. Owners with expertise are likely to have well-informed discussions with managers regarding the strategic direction of the firm. Managers are very likely to respond to large-block owners whom they regard as sophisticated, as expertise allows owner power to become legitimated—expected and desired rather than contested in the social context of corporate governance (Pfeffer 1981, Ocasio 1994).

Exploring Ownership Type

As we have outlined, there are many different “ownership types” of large-block investors: shareholders who have a seat on the board of directors, shareholders who sustain their ownership blocks over time, families, top executives, institutional investors such as public pension funds and mutual funds, LBO
and MBO associations, and venture capital funds (Kang 1996). They differ in the length of their involvement with firms, and their effect on performance depends on the industrial and competitive context in which the firm operates. We briefly illustrate how length of involvement and context may condition the influence of ownership types on performance.

We have already argued that length of involvement should be important for social influence and expertise of large-block shareholders, and long involvement should also make large owners more likely to assume positions of formal authority on boards of directors. For example, owner types such as family owners often have very long associations with the firms they originally founded. They should therefore gain considerable social influence and expertise as noted above. Family owners often "control" public corporations, where the extent of stock ownership by the controlling family affected managerial tenure (Allen & Panian 1982), family owners affect the susceptibility to takeover (Davis & Stout 1992), and family ownership suppressed adoption of the multidivisional form during the 1960s, but not during the 1980s (Palmer et al 1987, 1993).

Although many anecdotal accounts describe both high-performing and poorly performing family-controlled firms, there is a lack of theory and evidence on how family owners might affect performance in large publicly held US corporations. Research on the effect of large-block family ownership on performance in modern corporations has produced mixed results (Demsetz & Lehn 1985, Fligstein & Brantley 1992, Johansson 1993). One possible explanation for these mixed results is that the power that large-block family shareholders have may diminished over time as their formal authority, social influence, and expertise may decline in later generations. This "Buddenbrooks effect" occurs where early-generation family owners enjoy superior performance and make superior strategic decisions, while later-generation family owners do not enjoy superior performance and make less effective strategic decisions (Kang 1998b).

By contrast, other owner types are unlikely to develop a long history of social influence in the firm. This is the case for many institutional investors and LBO associations. The increased importance of institutional investors in particular has led some to suggest that US corporations may suffer from a "time horizon" problem, where managers are unable to make necessary strategic investments because of capital market pressures for immediate shareholder returns (Porter 1992). However, the price of publicly traded shares is thought to reflect the present value of all future streams of cash flows from the corporation, and empirical studies provide only anecdotal evidence on the "time horizon" problem.

The literature on corporate governance may further suggest that the effect of ownership type on performance is likely to be contingent on industry and
competitive context, as the formal authority, social influence, and expertise of each ownership type will vary contingent on characteristics of the industry and competitive environment in which the firm operates. Financial economic research suggests some industries are “transparent” where firms are relatively simple to monitor, whereas others are “opaque” where firms are difficult to monitor, based on whether or not capital and investments are highly firm specific (Zeckhauser & Pound 1990). Transparent industries, such as textiles and steel, are characterized by less firm-specific capital and investments, where most shareholders are more easily able to monitor managers. By contrast, opaque industries, such as microprocessors and pharmaceuticals, are those with highly specific capital investments, where most shareholders are unlikely to have the expertise and information necessary to monitor managers.

Certain types of large-block owners may be more able to increase firm performance under “transparent” industry conditions, whereas other types of large-block shareholders may be more appropriate for “opaque” conditions. For example, in the US textile industry, a “transparent” industry, large-block outside director owners, large-block owners who sustain their ownership over time, and large-block family owners each were found to be associated with increased firm performance (Kang 1996). By contrast, large-block owner-managers may be most effective in “opaque” industries, where their high levels of expertise and continual access to information allow them to participate effectively in corporate governance.

In addition, the social characteristics of industries may influence the effects of large-block owners on performance. In industries with a strong history of owner involvement, active participation of owners in corporate governance may be expected and accepted by managers, as political institutions and shared understandings of interdependencies, or “conceptions of control,” occur within each industry (DiMaggio & Powell 1983, Fligstein & Brantley 1992).

Firms also compete in industries that are emerging, growing, mature, or declining. The stage of the industry in this “corporate lifecycle” may influence how ownership structures affect firm performance. Research on venture capital firms indicates how these firms actively nurture and monitor startup companies through a series of stages (Sahlman 1990). Research on LBO associations have indicated how in declining industries with overcapacity, the discipline imposed by debt obligations combined with changes in management can lead to the creation of value (Jensen 1989).

Finally, the overall stability of the industry is likely to influence the effects of large-block owners on performance. Certain periods may be characterized by “environmental turbulence” (Haleblian & Finkelstein 1993) where industry shifts require strategic decisions that may reveal whether or not large-block shareholders “control” the corporation. Contingent on industry conditions, shareholders may have “active” or “latent” power (Herman 1981).
These important aspects of industry conditions may be developed into a "contingency theory of corporate governance" (Kang 1996), which suggests different types of owners are more or less effective at capturing property rights and increasing corporate performance, contingent on the specific industry context. Such a theory of corporate governance suggests that, one, there is no one best firm ownership structure, two, not all ownership structures are equally effective, and three, the best way to structure ownership depends on industry characteristics. This approach parallels Lawrence & Lorsch's work on organizational structure in Organizations and Environments, where they argue that, one, there is no one best way to organize, two, not all ways of organizing are equally effective, and three, the best way to organize depends on the nature of the environment to which the organization relates (Lawrence & Lorsch 1967).

Therefore, the "fit" between different types of owners and particular industry and competitive conditions then should determine the relationship between ownership organization and performance. A contingency approach to corporate governance offers an alternative to proposed solutions that assert certain investors, such as public pension funds, are ideal "active" investors across all industries (Pound 1992). The fit between different types of shareholders and firms may depend on the stage of the firm in the corporate lifecycle. Start-up firms often feature large-block ownership by founders, growth firms are often owned by venture capitalists, mature firms often feature family owners, and declining industries are often owned by LBO associations.

CONCLUSION

We have reviewed theory and evidence about ownership as an important sociological and organizational variable that affects firm performance. Nearly twenty-five years have passed since the "astonishing consensus" that managers, rather than owners, control modern corporations was found to be a social scientific "pseudofact" (Zeitlin 1974). However, the assumption of "managerialism" is again prevalent, as recent organizational research downplays the importance of ownership and instead focuses on other varieties of social structures, social relationships, and institutions that may constrain managers. Owners are now routinely depicted as fungible, where there is assumed to be virtually no social component in owner-manager relations. Although agency theory has brought important insights on the incentives of participants in corporations, its depiction of the corporation as being composed of principal and agent relationships has focused attention away from the interesting and important question of how power relationships develop among organizational participants. In particular, certain types of large-block shareholders may have sufficient formal authority, social influence, and expertise to capture property rights to gain control of the firm, giving them disproportionately large amounts
of benefit and use rights. Ownership types offer an alternative approach to measuring ownership structure purely in terms of ownership concentration, or simply classifying firms as owner-controlled or manager-controlled. The relationships between owners and managers have an important social dimension that cannot be expressed simply in contractual terms.

Our review suggests a contingency theory of corporate governance where the effect of ownership on firm performance is contingent on the “fit” between owner types and the industry context. Certain types of large-block owners may lead to increased firm performance, contrary to the “managerialist” assumption that ownership structure does not matter. We do not suggest managers are unimportant in determining firm performance. Historical accounts suggest a key failure of “personal capitalism” was that British enterprises controlled by owner-managers failed to employ the full staffs of professional managers necessary to govern the increasingly complex organizations, distribution channels, and production processes that characterized the Second Industrial Revolution (Chandler 1990). Corporations must employ highly skilled professional managers, but certain types of large-block shareholders may increase the effectiveness of these managers by shaping strategic decisions in ways that are associated with increased corporate performance.

The importance of studying ownership is likely to increase as the nature and structure of ownership continues to evolve in the US economy and in the world. Capital markets are possibly becoming increasingly efficient, with information on firm strategy and investment decisions more readily accessible to investors. At the same time, modern corporations have become less reliant on physical assets and are more dependent on intangible assets such as intellectual property and highly skilled employees who are often given ownership stakes as a form of compensation. Recent changes in ownership patterns are also likely to increase the importance of understanding the distributive consequences of the effect of ownership structure on performance, as the efficiency and distributive consequences of ownership are highly intertwined. Finally, although there may be a significant degree of “separation of ownership and control” in the United States, this is certainly not the case in most of the other wealthy economies in the world, where much of the theory developed on the Berle & Means corporation may only have limited relevance (La Porta et al 1998). Therefore, we conclude that ownership is an important but neglected sociological and organizational variable that deserves continued academic inquiry.
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