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Six Components of Corporate Governance That Cannot be Ignored

Joseph McCahery
Tilburg University
j.a.mccahery@tilburguniversity.edu

&

Erik Vermeulen
Tilburg University
e.p.m.vermeulen@tilburguniversity.edu

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Joseph A. McCahery
Tilburg University and ECGI

Erik P.M. Vermeulen
Tilburg University

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Keywords: board of directors, CEO, conglomerate, controlling ownership, corporate culture, corporate governance, corporate group, innovation, investor conference, investor relations, one-size-fits-all, shareholder engagement, widely dispersed ownership

JEL Classifications: G01, G32, G34, K20, K22, L22, L25, M14, O16

Joseph A. McCahery
Professor of Law
Tilburg University, School of Law
Warandelaan 2
Tilburg, 5000 LE, Netherlands
phone: +31-(0)13-466-2306, fax: +31-(0)13-466-2323
e-mail: J.A.McCahery@tilburguniversity.edu

Erik P.M. Vermeulen*
Professor of Business & Financial Law
Tilburg University, School of Law
Room M 820
PO Box 90153
Tilburg, 5000 LE, Netherlands
phone: +31-(0)13-466-8111, fax: +31-(0)13-466-2182
e-mail: E.P.M.Vermeulen@tilburguniversity.edu

*Corresponding Author

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Joseph A. McCahery[1] and Erik P.M. Vermeulen[2]

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Recent regulatory initiatives that attempt to encourage shareholder engagement, ensure board independence and improve the operation and transparency of corporate groups are of great interest to both academics and practitioners. These initiatives reflect a 'one-size-fits-all' approach that may lead to disappointing and counterproductive results and could destabilize and disrupt workable arrangements between management, the board of directors and investors. In this paper, we take a different perspective by showing how there is more to corporate governance than just providing protection to investors and other stakeholders. An important reason for corporate governance is that it also facilitates companies to be innovative, create value and maintain a competitive advantage. To show this, this paper focuses on six components that successful and innovative companies have in common. We support our argument with case studies to show how these companies have found different ways to give substance to the six components.

I. Introduction

Successful companies are companies that stand out from their competition in their approach to governance and ownership. What is remarkable is that they often challenge the conventional wisdom by deviating from what is generally accepted to be good corporate governance. Consider the composition, structure and operation of Apple's board of directors (Kane and Lublin 2010). In the 2000s, the board was relatively small and mainly consisted of friends of Steve Jobs. Currently, the absence of board diversity has caused it to attract additional corporate governance criticism (Satariano 2014). Board independence is also a concern at Walmart, particularly since the Walton family owns more than 50 percent of the outstanding shares on the company and the number of independent directors is declining (Dudley 2013).

[1] J.A.McCahery@tilburguniversity.edu. Department of Business Law and Tilburg Law and Economics Center, Tilburg University.
[2] E.P.M.Vermeulen@tilburguniversity.edu. Department of Business Law and Tilburg Law and Economics Center, Tilburg University.

While the above cases describe deviations from best corporate governance practices, another widely discussed deviation is the extent to which ownership is largely in the hands of insiders. Studies in the academic literature show that inefficient concentrated ownership is associated with a relative discount on the firm's share price. Anheuser-Busch Inbev, for example, has a number of shareholders that act in concert and represent more than 52 percent of the voting rights. Moreover, it is widely assumed that a conglomerate discount is applied to companies like General Electric (GE) and the Tata group (Stammers 2012). This discount is largely caused by the complexity of assessing the value of a company that is involved in a wide variety of unrelated businesses.

Another strand of the literature suggests that a valuation discount is not uncommon for groups that adopt a complex ownership. Stock markets apply a discount to Samsung and other family-controlled *chaebols* in Korea (Salmon 2007). This 'Korean discount' is usually explained by the lack of transparency and accountability in the *chaebols*, making them prone to minority expropriation. A competing view holds that *chaebols* have a valuation discount because of the market investors' response to the inclusion of low net present value (NPV) firms in the group (Almeida et al 2011). Moreover, this corporate governance 'problem' also exists in the world's biggest mobile phone operator, China Mobile, which is characterized by a majority state-ownership structure. Finally, efforts to increase transparency and protect minority shareholders are seen as responses to the corporate governance weaknesses in companies that have two or more classes of shares, such as Google.

Yet, despite a wide variety of unconventional corporate governance structures and market discounts, it is difficult to ignore the above-firms' success in setting record high share prices, thus indicating investors' trust and confidence in these companies. Consistent with this observation, the ownership and control characteristics of a business group can contribute negatively or positively to the long-term performance of the firm. We hypothesize that ownership and group structures are not the dividing line between 'good' and 'bad' corporate governance. Thus, it seems that a firm's continued ability to show a sustainable competitive growth may have a greater effect on investors and analysts than different types of corporate governance mechanisms.

We use the analysts' framework to assess the impact of a company's corporate governance structure.[3] We rely on three main elements. First, in order to secure long-term growth and value-creation, it is important that companies maintain sustainable competitive advantages over their market rivals. The long-term competitive advantage is referred to as economic moat (a term coined

[3] These elements are derived from Morningstar, a leading provider of independent investment research.

and popularized by Warren Buffet). The second element is uncertainty/risk associated with the firm's activities and future performance. The third, but less important, element is the firm's stewardship grade rating which is mainly associated with a company's capital allocation decisions.

To begin with, an assessment of the economic moat, uncertainty and stewardship grade provides valuable information about a company's prospects. On the other hand, a model that provides more insights on the effectiveness of corporate governance mechanisms that are material to a company's long-term growth and value-creation can contribute to the management of the business (OECD 2012a). For instance, the stewardship grade rating shows that the implementation of rules and regulations, particularly in the area of disclosure and related party transactions, may actually improve a company's investment strategy and increase shareholder value. However, the components that determine the stewardship grade rating are mainly related to the economic moat and uncertainty about a company' economical and technological prospects. However, it is far from clear whether other typically crisis-driven corporate governance considerations, such as independent directors, the separation of chairman and CEO, board diversity, active minority shareholder engagement, the disclosure of quarterly reports and, more recently in Europe, transparency regarding company group structures, are in fact truly material to a company's sustainable growth and value creation (Barton and Wiseman 2014). In this sense, it can be argued that the mechanisms are often perceived as 'nice-to-have' instead of 'must-have'.

The contribution of this paper is three-fold. First, this paper contributes to the literature on the effect of material corporate governance mechanisms on firm performance. While there is a large body of literature that examines the relationship between and index of a large set of corporate governance components and firm performance, there have been few studies that seek to identify the truly material corporate governance mechanisms by analyzing the economic moat, uncertainty levels and stewardship grade ratings of the world's largest (according to their market capitalization) FT Global 500 2013 companies (including companies from the United States, Europe and Asia). The findings in this paper show that these companies closely conform to six components, which we dub as the 'six Cs model'. We focus on the extent to which 'coordination', 'communication' and 'conversation' are important components at the headquarters' level. The group level is characterized by 'connection', 'collaboration' and 'co-creation'. Second, by introducing the concept of the 'coordinator', we contribute to the literature by highlighting the crucial and central role it plays in the corporate governance organization and structure of successful and competitive companies. Communication and conversation are supportive components that refer to both networks of investors and investor relations' strategies as well as network effects associated with brand loyalty and products. Connection, collaboration and co-creation are needed to increase a company's capabilities to team up with others (group companies, third party companies, governments and research institutions) to expand a company's market share, to produce products or services at a lower cost than competitors and to attract and integrate internal and external innovations.

Finally, we illustrate how the interactions and interrelations of the different components are imperative to a wide economic moat and low uncertainty level (and crucial for a firm's compelling financial performance supported by future growth prospects and a robust innovation pipeline). The ability of the coordinator to communicate these prospects clearly and effectively to the financial market is one example of the leadership skills critical to a firm's competing effectively. Consequently, the information enables investors to learn more about the firm, its management (and the people that make the company what it is) and the potential to keep competitors at bay. In fact, if a company fails to have an effective investor relations strategy, its stock may be perceived as slow growth and may in turn activate the demands of investors to implement shorter-term dividend and share buyback policies (Plender 2014). Arguably, once investors are committed to such a strategy, the usual result is that the company ends up in a vicious circle of non-material corporate governance discussions (McCahery et al 2013). In these situations, investors are likely to expect that firms will find it extremely difficult to recapture the long-term focus on deepening and widening the economic moat and reducing the uncertainty levels of the firm's businesses.

The paper is organized as follows. Section 2 distinguishes between truly material ownership structures and corporate governance rules and norms (that have a real impact on the way a company is perceived by investors, analysts, customers and employees) and non-material ones. Because we observe an increase convergence of crisis-driven corporate governance mechanisms across countries, and regulators should be mindful of the perils posed by overregulating corporate governance (Dignam and Galanis 2014), the question of which corporate governance structures and mechanisms are truly material to investors and other stakeholders is relevant to the current corporate governance debate. In order to answer this question and assess what really matters in corporate governance, Section 3 introduces six components of corporate governance, with a particular focus on the effect of these components on the economic moat, uncertainty and stewardship grade ratings. The analysis is supported by case studies and data derived from the FT Global 500 2013. Section 4 contains a summary of the analysis and offers several policy recommendations.

II. Material versus Non-Material Corporate Governance Rules and Best-Practices

Identifying a truly material mechanism in a firm's corporate governance structure can potentially be an important competitive advantage. Due to the often-presumed separation of ownership and control in listed companies, there is a presumption in the theoretical and empirical literature that the creation of standard and general mechanisms and other procedures is to curtail managerial misconduct and increase shareholder value. Equally, corporate governance frameworks typically contain formal provisions that seek to enhance the role of non-executive and independent directors, separate the role of chairman and chief executive officer, and implement risk management systems and strict disclosure rules. The rationale behind these mechanisms is to further develop financial markets and enhance investor (and other stakeholder) protection. Presumably, a stronger legal environment that better protects investors eventually causes the dispersion of ownership structures. However, a number of researchers have been critical of this narrow and crisis-driven corporate governance focus on discouraging the self-interested behavior of managers and promoting widely dispersed ownership structures (Bratton and McCahery 2001; Bruner 2011; Cossin 2012).

More recently, Larcker and Tayan (2013) argue that building an incentive system based on non-legal mechanisms, such as reputation and credibility, is associated with increased commitment, motivation and coordination inside firms. These findings suggest that a trust-based system, rather than a regulated framework (which attempt to target the 'worst offenders'), can play a major role in aligning the interests of managers, directors and shareholders and reduce the costs of firm's governance system. Other recent studies suggest, moreover, that the emergence of short-term holding periods, stock market fragmentation and dark pools may spur significant changes in legislation and a new approach to corporate governance (Isaksson and Celik 2013; Bianchi 2013). For example, an emphasis on stock price performance and liquidity encourages CEOs to focus on short-term results (Bolton and Samama 2012). Thus, the different factors that influence the choice of management to take a short-term view is one of the key challenges in the corporate governance debate (McCahery et al 2013).

In response to the short-term trend in capital markets, modern commentators have presented empirical evidence that corporate governance works best in companies that are controlled by one or more founders, a family or a group of actively engaged institutional investors, or belong to a business group. The basic argument is that 'controlling owners' have an incentive to establish and safeguard long-term commitments and trust within the company. Consider for example high growth companies, such as Google and Facebook, that have dual class share structures. To the extent that these capital structures are necessary to encourage the founders of these companies to continue to grow the business, they ensure stability over long time horizons (as stated in Google's 2004 IPO letter). Suppose that there is a lot of hype surrounding the initial public offering (IPO), dual class shares allow them to focus on long-term sustainable growth and value creation while offering resistance to the short-term attitude of the stock market.

The long-term focus arguably explains why controlling ownership structures continues to prevail in emerging markets despite the development of more effective legal environments and enhanced shareholder protection (which could cause ownership to disperse). This is reflected in Table 1 that provides a recent overview of the ownership structures in Asian countries (where families and the government are usually the controlling owners). In fact, family ownership is still the prevalent ownership structure around the world (Mayer 2013). The contemporary finance literature makes the claim that superior performance is attributed to a long-term investment horizon of the controlling family (Anderson and Reeb 2003; Villalonga and Amit 2006). Although there are costs associated to family ownership (e.g., the threat of private benefit extraction and tunnel vision), such a structure is arguably an effective mechanism to keep the family interested and directly or indirectly involved in the company's affairs, and may lead to greater benefits. It is acknowledged, however, that ownership structures are also dynamic, in that they (should) change over time according to evolving markets and shifting business strategies and practices, and may become less effective.

Table 1: Controlling Ownership Structures in Asia (based on the 20 biggest companies (according to market capitalization) in the Countries' main index)

Sum of Holdings of all 10 Biggest Shareholders										
%	China[4]	India	Indonesia	Malaysia	Philippines	Singapore	South Korea	Taiwan	Thailand	Vietnam
Mean	66.84	65.46	71.66	76.22	67.90	85.22	41.78	41.31	65.74	59.46
Median	64.35	69.46	70.69	74.83	67.39	86.18	42.30	42.06	64.90	65.35
Minimum	29.89	20.86	57.72	63.96	38.07	57.58	19.46	20.88	39.36	18.62
Maximum	92.35	95.44	90.07	90.98	97.07	97.88	67.68	89.49	87.92	85.80

Sum of Holdings of all 5 Biggest Shareholders										
%	China	India	Indonesia	Malaysia	Philippines	Singapore	South Korea	Taiwan	Thailand	Vietnam
Mean	61.52	58.42	67.82	70.94	62.85	76.84	36.25	33.22	59.47	55.19
Median	60.24	64.08	64.72	69.59	64.69	79.42	36.20	31.37	58.16	59.26
Minimum	21.86	13.03	47.97	58.06	31.78	48.80	14.48	12.70	35.95	17.77
Maximum	90.86	93.32	88.90	88.43	93.43	93.96	62.11	86.85	85.35	83.06

Source: Based on information disclosed in the 2012 annual report of the respective companies

[4] Note that 10 of the 20 companies in the sample are selected from the constituents of Shanghai Private-Owned Enterprises 50 Index (for the Shanghai Stock Exchange) and the other 10 companies are from Shenzhen SME and ChiNext 100 (for the Shenzhen Stock Exchange).

It is widely believed that the recent financial crisis may eventually lead to a revival of the conglomerate governance structure (Betts 2008; Economist 2014) (which was similar to controlling ownership structures viewed as an answer to underdeveloped legal systems and markets). In this case, the argument is mainly based on the fact that conglomerates from emerging markets, such as Samsung and the Tata group, have become serious competitors to their rivals in the developed economies. Empirically, there are also indications that point to a revival of conglomerate-type structures on a global scale (Woolridge 2012). In recent years, we have seen that there is a keen awareness on the part of large corporations of the need to invest in and/or acquire high technology startup companies that could not only spur their own innovation, but also provide opportunities to become active in markets that are somewhat distant from their current business (McCahery and Vermeulen 2010). To varying degrees, listed technology companies with strong balance sheets and cash positions are particularly active venture capital investors and acquirers of new innovations (Dittmer et al 2014).

Still the puzzle is why corporate governance discussions continue to focus on questions regarding superior ownership and control structures and 'one-size-fits-all' solutions and best practices that protect the interests of investors and other stakeholders. As noted, the drawback of the single recipe approach is that it fails to recognize that in general terms one structure is unlikely to be more effective than the other (and very much depends on a company's life stage and the sectors, regions, countries and cultures it operates in). Similarly, it is difficult, with little evidence, to draw general conclusions about the effectiveness of conglomerates. Much depends on the group centers' - the management of the group's headquarters - competencies, priorities and interactions with the entities within the conglomerate. Ramachandran et al (2013) distinguish between four types of business group centers: (1) the absentee landlord that is only interest in extracting rents, (2) the clan leader that only puts emphasis on the long-term identity/brand of the group, (3) the venture capitalist that focuses on growth and innovation, and (4) the evangelical architect that combines long-term identity with growth opportunities and strategy. Clearly, with the right structure, the business group can be an effective management arrangement for a portfolio of enterprises.

The 'one-size-does-not-fit-all' view captures what analysts value as important when assessing a company's inherent business and organizational characteristics as part of making their investment recommendations. For instance, Morningstar, a leading provider of independent investment research in North America, Europe, Australia and Asia, places weight on a company's economic moat, uncertainty and stewardship grade ratings (see Table 2). At first sight, the ratings are mainly influenced by factors outside the scope of corporate governance and ownership structures. For instance, factors that can deepen and widen the economic moat are market share, the patent pipelines, high customer-switching costs and network effects. The uncertainty is related to the predictability of future cash flows.

Take Google, the US Internet company, for example. On 31 December 2012, Google was essentially managed by three executives: Eric Schmidt (Executive Chairman of the Board of Directors), Larry Page (co-founder and Chief Executive Officer (CEO)) and Sergey Brin (co-founder and member of the board of directors). The executives owned approximately 92 percent of the outstanding class B shares, giving them about 65 percent of the firm's total voting power while their economic interest (cash-flow rights) was only approximately 20 percent. Most corporate governance experts see Google's dual-class ownership structure as a potential threat to investors. The first and main argument against control-enhancing arrangements is that the immediate creation of shareholder value is usually not the main priority of the executives. Second, the use of restrictive control rights often makes managers prone to tunnel vision. Third, prior research on these issues has focused on how the dual-class share structures provide ample opportunity for insiders to act self-interestedly at the expense of other investors and stakeholders.

Table 1: Important factors that determine economic moat, uncertainty and stewardship grade

Economic Moat ***Ratings: wide, narrow, none***	**Uncertainty** ***Rating: low, medium, high, very high, extreme***	**Stewardship Grade** ***Ratings: exemplary, standard and poor***
Huge Market Share	Sales Predictability	Investment Strategy
Low-Cost Producer	Operating Leverage	History of Investment Timing and Valuation
Patents, Copyrights or Government Approvals and Licenses	Financial Leverage	Financial Leverage
Unique Corporate Culture	A Firm's Exposure to Contingent Events	Dividend and Share Buyback Policies
High Customer-Switching Costs		Management Compensation
The Network Effect		Related Party Transactions
		Accounting Practices

Source: Adapted from Morningstar

However, analysts have long understood the importance of taking a broad approach to assessing Google's corporate governance. For example, they appreciate the deviation from a one-share-one-vote system. The multi-class share structure clearly allocates control to the founders and exposes them to the business world, which in turn provides the necessary incentives to focus on accelerating sustainable growth and value-creation (thereby widening the economic moat and reducing uncertainty). There is little doubt that forcing the founders to accept a predetermined corporate governance mold will have a counterproductive effect. Similarly, analysts are also comfortable with a management's long-term focus on capital allocation. Such a governance practice is prevalent in the recent acquisitions of high-tech companies including DoubleClick, Android and YouTube. Furthermore, analysts are of the view that a 20 percent economic ownership is likely to align the interests between the executives and Google's investors. From their perspective, it is clear that, because the competition for talented employees is fierce in the technology sector, Google executives take shareholder value very seriously. Hence, a positive stock price performance will not only reduce the cost of capital, but also (and more importantly) make it easier to attract and retain talent with the common 'retention tools', such as restricted shares and stock options. Unsurprisingly, the investors in Google allowed for the recent introduction of a new class of non-voting shares that would be distributed to existing shareholders in a 2-for-1 stock split without diluting the founders' voting power (Farzard 2014). As Table 3 illustrates, Google has a wide economic moat that can help ensure returns on capital and, like most companies, a standard stewardship rating. At the same time, it is important to underscore that the fierce competition and low switching costs are the main reasons for the high uncertainty rating.

Nevertheless, corporate governance experts estimate that part of the significant uncertainty and standard stewardship grade rating of Google is attributed to the owners' increased ability to employ strategies to extract resources and assets from the firms they control. These include dilutive share issues, insider trading, withholding important information and related party transactions (Vermeulen 2013). This governance risks appear particularly true for shareholder structures that give the owners control rights in excess of their cash-flow rights (IRRC/ISS 2012). Unsurprisingly, a large body of literature is devoted to the design and analysis of corporate governance mechanisms (such as rules, regulations and norms) that prevent opportunistic behavior on the side of the controlling owners. Thus, as we have seen, there is no clear-cut answer to the question of whether these mechanisms are truly material. The evidence, moreover, suggests that the recent crisis-driven and one-size-fits-all corporate governance frameworks and structures appear to play a very limited role and therein lies the problem of identifying how successful firms differ from less successful ones in terms of governance. Managers, investors, analysts and other stakeholders often accept deviations from the conventional corporate governance model. Still, one clear area of consensus across the board is that related party transactions and beneficial ownership rules and regulations are material in limiting controlling shareholders from opportunistically expropriating private benefits of control while at the same time widening the economic moat. This will be discussed in the next Section.

1. Material: Disclosure and Related Party Transactions Rules

There has been a surge in research that suggests corporate governance is overrated. Yet there is little evidence to support this view. For example, analysts and investors when assessing the stewardship grade ('exemplary', 'standard' and 'poor') consider related party transactions and accounting practices to be truly material. On a very general level, related party transactions can play an important and legitimate role in a market economy (McCahery and Vermeulen 2005). For firms, trade and foreign investments are often facilitated by inter-company financing transactions. Lower costs of capital and tax savings provide a strong incentive for companies to engage in these transactions. There are many examples of related party transactions that yield benefits for companies. By far the most popular transactions include: (1) inter-company loans or guarantees from parent to foreign subsidiaries; (2) the sale of receivables to a special purpose entity; and (3) a leasing or licensing agreement between a parent and a foreign subsidiary.

However, a key concern about related party transactions is that they might not be undertaken at 'arms-length' market prices but can be influenced by the relationship between the two sides of a transaction. For both controlling shareholders and insiders (such as the executive managers), related party transactions can then become a mechanism for extracting private benefits of control at the expense of minority investors and other stakeholders (such as employees and third party creditors). It is therefore not surprising that most jurisdictions around the world have gradually implemented a variety of legal strategies in their corporate governance frameworks that regulate related party transactions and address or mitigate conflicts of interests. The legal strategies can be divided in three major categories (McCahery and Vermeulen 2008): (1) rules that require disclosure of related party transactions, (2) rules that require the approval of shareholders and (3) rules that prohibit certain related party transactions.

Because the attempt to identify related party transactions often raises complex issues that cannot easily fit into a set of prescriptive rules, the legal systems of most jurisdictions around the world contain general principles (such as those of the International Accounting Standards Board, which define related parties as well as determine the scope of related party transactions) to identify related party transactions. According to IAS 24, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related party transactions are defined as a transfer of resources or obligations between related parties, regardless of whether or not a market price is charged. The OECD Principles of Corporate Governance (2004) and most of the securities regulations around the world take a comparable approach and state that related parties can include entities that control or are under common control of the company, its board members, and significant shareholders, including members of families and key management employees (OECD 2012b).

To appreciate the challenges relating to the regulation of related party transactions, it is necessary to have a clear picture of the control and ownership structure of the companies. Legislatures have introduced clear and stringent disclosure and transparency obligations that reveal the identity of the persons who should be considered as the ultimate beneficial owner. When should disclosures be made? Although there are some variations across jurisdictions (particularly with respect to the disclosure thresholds), one of the most important governance mechanisms is the disclosure of the beneficial owner of more than a certain percentage (usually five percent) of certain equity securities to disclose information relating to such beneficial ownership (Vermeulen 2013). On the issue of scope of disclosure, it is mandatory usually for investors to disclose shareholder agreements and acting in concert arrangements if they together with the other shareholders exceed the legal threshold for holdings of the outstanding shares of the company (Jurdant 2013).

Given the importance of disclosure rules and related party transaction regulations, there is a high degree of formal convergence of the legal and regulatory requirements in these areas. Indeed, it is widely acknowledged that information about the ownership structure and the prevention of opportunistic behavior is truly material to investors. The Google example lends support to this view. In this context, investors were only able to appreciate the dual class shareholding structure after it had been adequately and properly disclosed. Underlying this account is the view that disclosure promotes investor confidence and the valuation of the investment. Nevertheless, it could be argued that the sheer implementation of the disclosure and related party transactions rules and regulations is not sufficient. The emphasis on enforcement systems to ensure that companies comply with the material corporate governance rules and standards is equally important. This is exemplified by the Korean Conglomerate and tech giant Samsung, which we will elaborate on in the next section. Also, and perhaps more importantly, the Samsung case describes how 'new' corporate governance components relate to growth and innovation appear more useful to investors and other stakeholders in assessing a company's economic moat and uncertainty level than the compliance with the crisis-driven (and principal-agent focused) mechanisms.

2. A Material - Non-Material Corporate Governance Conundrum: Samsung

In a snapshot, Samsung is the largest family-controlled multinational conglomerate (*chaebol*) in Korea. It comprises a number of listed and non-listed subsidiaries and associated companies that (although they operate in a wide variety of sectors) are bound together through a network of cross-ownership structures. Some of the most notable companies are: (1) Samsung C&T Corporation, a listed construction and trading company that was one of the main contractors for building Tower 2 of the famous Petronas Towers in Kuala Lumpur and (2) Samsung Electronics, the electronics and information technology company that is considered to be the flagship of the Samsung *chaebol*. In this paper, we focus on the latter company.

Samsung Electronics Co., Ltd was established in 1969. Its shares are floated on the Korea Stock Exchange since 1975. On 31 December 2012, it consolidated 166 subsidiaries that were mainly located in Korea, China, Europe and the United States. Current research suggests that the financial market (investors and analysts) has a love-hate relationship with Samsung Electronics. Let us first focus on the 'love' aspect. Between 4 January 2000 and 15 January 2014, the stock price soared from KRW 305,500 to KRW 1,299000, increasing 325 percent. The 'love' relationship is confirmed by the relatively high proportion of analysts who usually give Samsung Electronics a 'buy' rating. Thus, the importance of being part of a family-controlled conglomerate appears to offer several advantages that have a deepening and widening affect on the economic moat and reduces the uncertainty level. Additionally, it has the ability to create a unique corporate culture (which is not easily replicated by non-conglomerate multinationals) in which business opportunities are adequately shared among the company's business units and the diversified group of affiliated companies that belong to the conglomerate. Affiliated companies are, for instance, Samsung Heavy Industries, Samsung Fine Chemicals, Samsung Venture Investment and Samsung Engineering.

The unique corporate culture is also persevered through the key executives of Samsung Electronics. The current Vice Chairman and CEO, Oh-Hyun Kwon, has been with Samsung for almost 30 years, working his way up from the semiconductor business to CEO in 2011. His long tenure and experience give investors sufficient confidence that he will make decisions that help maintain Samsung's position as an industry leader in various categories. This perspective is useful for understanding that Samsung's CEOs generally have a good 'business' reputation. For instance, a recent study shows that Yun Jong-Yong (who was Samsung Electrons' CEO from 1997 to 2008) occupies the third position (after Steve Jobs (Apple) and Jeffrey P. Bezos (Amazon)) in the '100 Best-Performing CEOs in the World' ranking which is based on the total shareholder return (Hansen et al 2013).

There is also other evidence that investors appreciate the fact that Samsung Electronics operates two business units through which it controls the development, design and manufacturing processes behind its successful smartphones: the DMC and DS divisions. The first division includes the Consumer Electronics business (digital TVs, monitors, and domestic appliances) and the Information technology & Mobile Communications business (mobile phones, communication system, printers and computers). The second division consists of the semiconductor business and LCD display panels and OLED panels designed for mobiles in the LCD and other LED business. The importance and value of the interconnectedness between the divisions is the foundation of Samsung's competitiveness position. First, it provides the ability to produce products, such as their smartphones, at a lower cost than its main competitors. Second, it also enables Samsung to introduce new and innovative products faster than its main competitors. It could, for instance, be argued that these advantages provide a basis for the hypothesis that Samsung has rapidly increased its competitiveness in the mobile phone market, which resulted in Apple being gradually relegated from the 'first mover' to the 'follower' position

As noted, there is not only 'love' between Samsung Electronics and its investors. In fact, the 'hate aspect of the relationship' was recently reinforced when Samsung announced its uninspiring fourth-quarter 2013 results. Can these results be interpreted as predicting slower growth (Back 2014)? Indeed, the smartphone sales by its CE division were down nine percent from the previous quarter. The profits were also declining and the quarterly growth was the slowest since the third quarter of 2011. Moreover, the pressure from Chinese competitors, which are increasingly able to produce low-costs smartphone models and the expectation that Apple is on the brink of introducing a larger screen iPhone, exacerbated investors' uncertainty and narrowed the economic moat. Notably to ameliorate these results, Samsung, was being encouraged to embrace governance-focused reforms. We consider whether these measures could restore investor's trust and confidence and, in turn, assess other measures' ability to deliver a return.

The first proposed reform was based on corporate governance experts who have suggested that the web of cross-shareholdings (which give controlling families the opportunity to maintain and enhance control in excess of their economic interests) should be unraveled. This 'one-share-one-vote' approach would improve the checks-and-balances in the corporate governance incentive system, which would make it more difficult for the families to destroy shareholder value and divide executive positions among their members (Mundy 2012).

The second proposal was that Samsung Electronics should introduce a more rigorous and investor-friendly dividend and share buyback policy. Ironically, it paid a significant bonus of approximately US$ 745 million to its employees during the fourth quarter of 2013 to 'celebrate' its 20th anniversary of the 'strategy-changing' speech by its 72-year old Chairman Lee Kun Hee (Mundy et al 2014).

Finally, the third proposal suggested that investors rely on Samsung Electronics' executives to coordinate (as suggested by its Chairman) the exploration and exploitation of new business - more 'software-oriented' - areas. Samsung's collaboration with Intel to co-create a new operating system for mobile devices is arguably an initial step in this direction. The same could be said about Samsung Venture Investment Corporation, which actively seeks to get connected to the future-oriented businesses and innovative technologies in the areas of software and internet by investing in high-tech companies.

In this case, it is anticipated that the third proposal has most positive impact on the economic moat, uncertainty and stewardship grade ratings. The first two proposals could be designated as 'corporate governance' proposals. While on the surface these proposals have some appeal, they do not seem material to Samsung Electronics' innovation, growth and long-term value creation potential. Even though corporate governance theorists have long focused on the implementation of 'one-share-one-vote' and dividend/share buyback arrangements, these initiatives could even have a destructive effect on the growth perspectives. The third proposal appears to have some merit, particularly for the economic moat. According to stock analysis service Trefis, 42.6% of Samsung Electronics' stock price could be allocated to its mobile phone business in 2013.[5] It is crucial for Samsung to increase the switching costs and networks effects for its products. To anybody even vaguely familiar with the mobile phone industry, it is obvious that an effective way to do this is to develop and introduce a proprietary operating system platform (currently Samsung devices operate on Google's Android software).

It is important to reiterate that Samsung's shift towards the software business, together with the competitive advantages of being part of a strong conglomerate with a focus on research and development, should create ample sustainable and long-term growth opportunities. However, more is needed (than products and technology) to successfully address the recent pressures from the investor community. In January 2014, Samsung Electronics shares traded at a remarkably low price (with a price-to-earnings ratio of approximately 6.5). Although governance experts put most of the blame to the poor corporate governance system of Samsung, the prime cause of the discount (which is labeled as the 'Korean discount') is more likely to be associated with the lack of transparency of ownership of the company that makes it extremely difficult to determine the company's value and detect abusive related party transactions. The fact that the Chairman has

[5] The stock price allocation of Samsung Electronics is as follows on 5 March 2014: (1) mobile phones 42.6 percent, (2) DRAM & NAND Memory 20.7%, (3) Flat Panel Displays 9.4 percent, (4) TVs, Laptops and Other Appliances 4.3 percent and (5) cash (net of debt) 22.9 percent. See www.trefis.com (2 February 2014).

been convicted of paying bribes to government officials in exchange for government contracts and tax evasion, but was able to receive a pardon in both cases, does allegedly not contribute to the investor confidence (Yang 2012).

So, what can be done to increase Samsung's ownership and governance transparency? Ultimately, Samsung Electronics seems to be aware that the responsibility for implementing disclosure policies lies to a large extent with the companies themselves. For example the second 'Samsung Analyst Day' was held on 6 November 2013 in Seoul in an attempt to boost its stock price. Note that the first analyst day took place on 3 and 4 November 2005 (Cheng 2013). Even though Samsung has no impressive track record when it comes to organizing investor events itself, it regularly visits and presents at investor conferences that are organized by investment banks. The investor conferences and other events clearly add to Samsung's 'investor friendliness', which in turn has a positive effect on the stewardship grade. However, it does not sufficiently restore or improve investor confidence. What are the primary factors that give investors confidence? As discussed, information about the ownership and control structure - that companies are legally required to disclose to the public - is necessary for investors to make well-considered investment decisions. In addition, adequate and proper enforcement systems are crucial to ensure compliance with the rules. What is noteworthy in this regard is that in instances where proper accounting and disclosure standards are lacking, a dual listing, for instance a listing of depository receipts (ADRs) in the United States, could provide ancillary benefits as well. Listing requirements that require strict adherence to accepted disclosure and accounting standards offer tangible benefits to entities and can directly lead to improvements in investor confidence (and attract more foreign investors to its community) as a consequence.

In this Section, we have introduced Warren Buffet's economic moat to the corporate governance debate. We have assessed the principal benefit of corporate governance and draw the following conclusions. First, companies (particularly their executive managers and board of directors, but also their investors) may be partially responsible for the short-term mentality within their organizations and the investor community. Yet, they are also crucially part of the solution. Second, the empirical evidence shows that investors and stakeholders appear to appreciate diversity in corporate governance structures when it is related to future growth, innovation and value creation. It is therefore remarkable that most recommendations and best practices are general, attempting to capture the corporate governance framework in a one-size-fits-all model. This leads to the question of whether we can define new corporate governance indicators, best practices and strategies that respect the diversity (other than related party transactions and beneficial ownership rules and regulations), while also promoting sustainable long-term growth and value creation in companies? We attempt to answer this question in the next Section.

III. What Is It About the Successful Companies?

In 2011, Edward Glaeser made an interesting observation that: '(a)mong cities, failures seem similar while successes feel unique' (Glaeser 2011). We can interpret Glaeser's reasoning as applying also to companies since they arguably have a strong resemblance to cities. The typical response to corporate failures and scandals is the introduction of more stringent 'one-size-fits-all' and agency-based rules and regulations. Some of these new regulations may be more effective for some than others. At the same time, we take the challenge of the success stories of Samsung and Google to suggest that policymakers, academics and practitioners might change their approach to what is good or bad governance and be more reluctant in deriving 'one-size-fits-all' conclusions about the most effective ownership, control and governance structures. As we have seen in Section 2, ownership is firm specific and varies for instance across life stages, sectors, regions, countries and cultures.

Successful companies, like all prosperous cities, have also something in common. To thrive and stay one step ahead of their competitors (economic moat), companies must coordinate research and development (R&D) and operations to accelerate product/service innovation, be able to deliver products or services at a lower cost than competitors, and meet customer demand. To reduce uncertainty, companies must also connect, collaborate and co-create with other internal (inside the company) and/or external parties. Finally, to receive an exemplary stewardship grade rating, it is necessary to initiate investor-management conversations to disseminate information about a company's growth prospects, which, if communicated well, are usually considered to be a competitive advantage for companies. These arguments illustrate why companies that are already world-leaders in their respective markets are generally open to their investor community.

How do successful companies, with diverse strategies, deal with coordination, communication, conversation, connection, collaboration and co-creation. In this Section, we describe the 'six Cs' strategies of different successful companies and their impact on economic moat, uncertainty and stewardship grade ratings. We then investigate the top firms and proxy for this by comparing the top-20 companies that appeared in the FT Global 500 2013 list. We also document that, as Table 3 provides, there is no one formula for a proper corporate governance framework, the components of which are usually highly sector, country and company specific. We focus here on this comparison since it allows us to better understand the common denominator in the governance structure and organizational strategies of successful companies.

1. The Coordinator

The essence of the CEO's function is change of wealth of the shareholders by maximizing the share price of the company's stock. Yet with the increase in firm size and complexity, the top executive functions now include the coordination of activities across different business units. In this section, we canvass the ways in which the coordination role of top executives is truly material to high performing and competitive companies.

The logic of the coordinator's role is that it provides a link between the investor community, the business divisions or business units and the customers or society. The contribution of the coordinator is to set the parameters for innovation and business, marketing and operations strategy within a firm. Coordination that is successful and institutionalized may evolve into a unique corporate culture and 'tone-at-the-top' that helps a company or group of companies establish (and maintain) a wider economic moat. The coordinator's role is usually unique to companies or group of companies, but the role is not set in stone. To the extent that a company (or group of companies) is gradually becoming an 'ageing giant', a well-performing and adaptive coordinator that initiates strategies that, for example, increase productivity and/or spur innovation can turn themselves into a successful healthy ageing model in the corporate life cycle.

The coordinator is reflected in the fact that certain functions are not required to be performed by one person. Presumably this is the case in relatively young high growth companies. For example, Google is noteworthy since it is clear that the coordination role is played by the executive managers. In more mature companies, a family (with its specific family values and norms) or a group center is often in charge of coordination. The factors that account for the success of the coordinator's role include not only a focus on strategy, but also the branding of the firm's products and services. Tata is an example of a corporation in which its success is largely attributed to the fact that its group center is committed to a smart mix of branding and strategy work (Ramachandran et al 2013).

In addition, the coordination role can be institutionalized or supported through the establishment of mission statements and the implementation of compelling corporate values, practices and programs (Coleman 2013). An example is Walmart's 'every-day low-cost' proposition. Analysts view this proposition as an intangible source of economic moat, particularly since Walmart communicates the 'every-day low-price' message on a regular basis to its core customers (which is perceived as showing its dominant position in the market). The Walmart example also shows that it is difficult to reorganize/change a successful and effective 'coordinator'. Although the CEO of Walmart spearheaded a repositioning attempt ('project impact' which mainly focused on the shopping experience instead of price), it was not accepted by Walmart's customers and was dropped. To be sure, such problems are not limited to repositioning a project.

One of the common challenges that many companies face is linked to how to maintain or restore an active and adequate 'coordinator' This is exemplified by the fact that the board of directors of Microsoft needed more time to find Steve Ballmer's successor than expected. Structurally, Steve Balmer, who has been with Microsoft since 1980, is one of the pillars of the 'coordinator' that operates in the company. Bill Gates, the founder and Chairman of the board, is another pillar. Together they owned 9.4 percent of the outstanding shares in 2013. Apparently investors view this as sufficient 'skin in the game'. Given investor expectations, it was not surprising that company incumbent, Satya Nadella, was eventually named as the new CEO on 4 February 2014. Bill Gates and Steve Ballmer remained directors. Even though Bill Gates stepped down as Chairman of the board, investors expected that his role as technology advisor to the company and its new CEO would get him more involved in the future strategy decisions within Microsoft. But, it remains to be seen if Bill Gates' more central and active role in Microsoft improves and strengthens the coordination system. Investors were not immediately convinced and decided to pursue a wait and see approach (Foley and Waters 2014).

Family controlled companies that face large risks also find it difficult to maintain the role of the coordinator. In these companies, the coordinator usually consists of family members or their representatives. Once again we see that the coordinator's success depends on how well the strategy and branding functions are performed. In well-functioning family firms, it is important that the 'coordinator role' will be protected and preserved through succession arrangements. However, given the dynamics of and interrelation between the business, ownership and family-related factors in family firms, it is usually difficult to implement effective corporate governance mechanisms that create credible commitments and encourage growth and value creation (Claessens et al 2002; McCahery and Vermeulen 2008). The risk is if the family is only self-interested without paying attention to the company's branding activities and strategies (that ensure a sustainable growth and value creation), it is often necessary to initiate a reorganization or restructuring process (e.g., an acquisition by private equity parties) to restore or reinvigorate the 'coordination focus'.

Table 3: Who/What is the Coordinator?

Company	Economic moat	Un-certainty	Steward-ship Rating	Coordinator
Apple	Narrow	High	Standard	'Steve Jobs' leadership and creativity (Apple appears to struggle with restoring or changing the coordinator role) (Kane 2014).
Walmart	Wide	Low	Standard	Walton family supported by 'every day low cost' brand.
General Electric	Wide	Medium	Standard	Strong CEOs (Jack Welch was Chairman and CEO from 1981-2001/Jeff Immelt Chairman and CEO since 2001) – The CEO implemented a strong Corporate Culture which is adaptive to the ever-changing business environment (Brady 2005).
Microsoft	Wide	Medium	Standard	Chairman and founder Bill Gates and 'inside' CEOs.
IBM	Wide	Medium	Exemplary	Corporate Culture/Company Veterans.
Nestle	Wide	Low	Standard	Corporate Culture/Company Veterans.
Johnson & Johnson	Wide	Low	Standard	CEO change in 2012 has not changed the coordinator function. Coordinator role is institutionalized through strong brand supported by intellectual property, making it an attractive partner for innovative start-up companies.
Samsung Electronics	Wide	High	Standard	Chairman/*Chaebol* (but more disclosure required) supported by a innovation culture, leading to new products and intellectual property (Davies 2014).
China Mobile	Narrow	High	Standard	Government ownership and management (but more disclosure required).
Google	Wide	High	Standard	Executive Chairman and Co-Founders (protected by the dual class share structure).
Procter & Gamble	Wide	Low	Standard	In the process of restoring the coordinator function and renewed focus on growth and innovation (explains involvement of hedge fund).
Pfizer	Wide	Medium	Standard	Corporate Culture/Company Veterans.
Roche	Wide	Low	Standard	Novartis and a group with pooled voting rights (non-voting shares are issued to the public).
AT&T	Narrow	Medium	Standard	CEO and Chairman (Randall L. Stephenson used AT&T's strong competitive position as a provider of landline to transform to the company into a multiplatform telecoms provider by setting up collaborations with other large companies, such as IBM and Apple).
Novartis	Wide	Low	Standard	Company established through a merger between Sandoz AG and Ciba-Geigy AG in 1996. Dr. Vasella built a healthcare conglomerate, by diversifying the company into a number of new healthcare businesses and focusing on innovation. After 25 years, Dr. Vasella stepped down as Chairman after the company had reported disappointing results in 2013. In 2014, the company attempts to 'reinvent' the coordinator role (the current CEO and Chairman) by creating a more focused healthcare company. The strong patent and innovation pipeline enables the 'new leaders' to make the transformation without being too disruptive to the corporate culture (Falconi 2014).
Coca-Cola	Wide	Low	Exemplary	Brand and heritage (Coleman 2013).
Toyota Motors	None	High	Standard	"The Toyota Way" (Liker and Convis 2012): built on strong foundation of innovation and customer-focused improvements (Toneguzzi 2014). The current CEO, Mr. Toyoda (grandson of the company's founder) attempts to add more flair to the Toyota way.
Anheuser Busch Inbev	Wide	Medium	Exemplary	Tried and tested 'repeatable' business model with a strong focus on cost cutting (Allen 2012).
Oracle	Wide	Medium	Standard	Founder (and Deep Management Team).
Philip Morris	Wide	Medium	Exemplary	Chairman and CEO's strong focus on emerging markets (supported by collaborations and a strong brand in countries where smoking is not taboo) .

Source: FT Global 500 2013 (excluding oil and gas producers and financial institutions), Morningstar, Company Websites

Family businesses face other challenges. The first is the strategic challenge involved in transition and succession planning. The second is generational change that may increase the probability of a break down in the family business. Thus, after the third generation, mechanisms that create ‘mutual hostage’ situations will often be introduced to encourage family members to work through the differences that could negatively affect the coordination function. Many of the most successful family-owned businesses, in fact, employ a variety of mechanisms to tie family members for generations. For instance, lock-in provisions make it virtually impossible for family members who wish to liquidate their interest by exiting the company. Common ‘penalty’ mechanisms include the right of first refusal to family members on tendering shares, below-market valuations in the case of a share buyback, and restrictions on the number of shares that can be sold in a particular period. At the same time, surveys show that family members create institutions and privileges that function to align the family interests with the business interests, thereby minimizing conflicts. And indeed the evidence shows that families typically anchor their members through large charitable organizations that offer employment to members not yet active in the business and include decision-making opportunities for the children of family members (Elstrod 2003).

Generally, the coordinator’s role can be preserved in family firms by treating the two life cycles – the business and family life cycle – separately. As it happens, best practice is to create separate legal institutions to permit an isolation of issues without sacrificing unity. To be sure, business decisions will be affected by certain developments within the family and vice versa. However, the establishment of, for instance, a Family assembly, Family Council and/or Family Constitution furnishes parties with the opportunity to discuss family matters, such as family values and employment policies, without directly influencing business decisions and causing deadlocked issues. Dealing with emotions in a more informal setting has the advantage that a much more elaborated business strategy, in which family values are maintained, can develop. Family institutions thus have a prophylactic effect in that they help avoid disputes and conflicts. Other mechanisms in family business charters include the design of the board and the composition of its members, the voting rules and appointment procedures, the conditions for family members’ participation in firm decision-making, their role in the business and succession planning, and the dissemination of information and dividends (McCahery and Vermeulen 2008).

A more complicated exercise is to reinvent or restructure a ‘once’ effective ‘coordinator’ in times of crisis. What does it mean for a coordinator to be labeled ineffective? During their life cycles, it often occurs that highly successful companies lose their mojo and competitive advantages to other companies due to, for instance, economic headwinds or disruptive technology shifts. IBM is a clear and well-known case. In 1993, after the company reported a loss of more than US$ 8 billion, IBM was labeled as a dinosaur that was on the brink of extinction. What could be done to successfully turn the company around? Although there is no one-size-fits-all answer, a typical solution is to appoint a new CEO. Unsurprisingly, IBM followed this common procedure and appointed Louis V.

Gerstner Jr. who was recruited from outside IBM (which was a clear deviation from the typical CEO succession planning process within the company). Besides going through the necessary and often dramatic reorganizations (such as reducing the workforce from approximately 370,000 employees in 1990 to a bit more than 220,000 employees in 1995), IBM's new CEO made a remarkable and often undervalued decision (DiCarlo 2002). Because having chosen to reposition IBM by making all the different units and country organizations connect, collaborate and co-create, he avoided splitting up the company and destroying the unique and valuable corporate culture (Gerstner 2002).

Clearly, the focus on connection, collaboration and co-creation tremendously streamlined the innovation process, stripped layers of complexity and introduced a shared-services model, which enabled IBM to make better use of their resources and talents (Van Kralingen 2010). Perhaps the most important lesson from Gerstner's reorganization exercise is that if a company's brand, product or services are not competitive enough to cope with the business challenges (before 1993 'no one ever got fired for buying IBM), coordination can only be effective if it is tightly integrated from top to bottom into the corporate culture through connection, collaboration and co-creation between a company's business units and the outside world (see Figure 1). Nevertheless, there is no ideal type solution for companies that are going through tough times. Each coordinator's problems, challenges, complexity and culture are unique. Also, we expect a difference in the components that are integrated in the coordination system across companies.

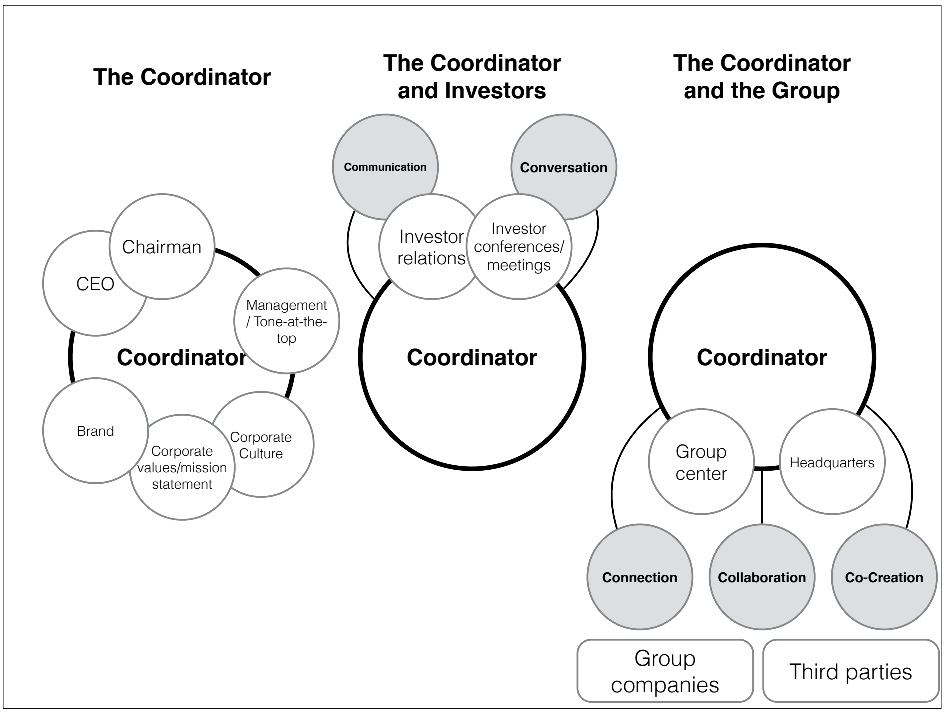
Do these arguments about the coordination system also apply to ownership and control networks outside the United States? Consider, for instance the Japanese multinationals, which experienced explosive growth in the postwar period (1950s to 1980s), but are currently facing fierce international competition and stagnation (Araki 2012). Alarmed about the erosion of competitiveness in foreign markets, Japanese firms increasingly rely on sales in the domestic market. In order to turn this around and widen the economic moat (by becoming more international), the 'Japan Inc.' companies started to appoint foreign CEOs. However, many firms have found it difficult to implement the desired changes successfully. Evidence shows that foreign CEOs stumbled and struggled in their efforts to alter Japanese corporate culture (Voigt 2012). In many cases, the attempt to transform the (often unique) culture to open the way for innovation and sustained profitability may partly explain the failed initiatives of foreign CEOs to lead Japanese companies. Yet this may also explain the success of Carlos Ghosn, the French-Lebanese-Brazilian CEO who was actually able to turn around Nissan Motor Corporation.

Carlos Ghosn, who was named CEO of Nissan Motor Corporation in 2001, quickly (in two years) transformed the loss-making car manufacturer to a profitable enterprise by respecting the Japanese corporate culture and connecting with people within the organization (Todd 2005). Arguably, it was his ability to successful conform to Japanese business etiquette that made it possible to close plants and halve the number of suppliers. More importantly, because of this respectful approach to the reorganization and restructuring process, he was able to challenge Japan's lifetime employment system by significantly reducing the number of employees on the payroll of Nissan Motor Corporation. In a Wall Street Journal interview on 17 November 2009, Ghosn stated in fact that the significant reorganization was only successful because the management team (particularly the CEO) showed compassion and commitment and paid attention to people (particularly to the ones that had become redundant). In short, Carlos Ghosn realized that respect for the existing and integrated coordination process and corporate culture is a necessary condition for making reorganizations and business changes a success (Ogilvie 2009).

Recently, Mr. Ghosn seems to have experienced a sudden and unexpected loss of touch in how to handle corporate culture and tone-at-the-top issues (Harner 2013). Nissan Motor's shares sunk after a profit warning in November 2013. A plausible explanation for the share price decline is the CEO's drive to make Nissan a global car manufacturer. According to newspaper the Nihon Keizai Shimbun, 79 percent of the cars are manufactured outside Japan in the period between April and September 2013. Also, R&D activities have been slowly but surely relocated to foreign countries. We can distil from the later example that if globalization and relocation activities interfere too heavily with the existing corporate culture and coordination function, they are likely to have a detrimental effect on the performance and growth prospects of a company.

Our discussion of coordination (and the importance of the coordinator and corporate culture) also underscores the importance of board dynamics and having a well-balanced board (McCahery and Vermeulen 2014). In order to make a company adaptive to global competition, it is important that boards challenge the coordinator and, more importantly, support coordination activities by identifying opportunities and networking with governments, society and other stakeholders (Cossin 2012). Using this framework, consider Toyota Motors' recent decision to appoint three real independent directors (which was approved by the shareholders in June 2013). Ikuo Uno, an adviser to Nippon Life Insurance Co., Haruhiko Kato, president and chief executive officer of Japan Securities Depository Center Inc., and Mark Hogan, a former group vice president at General Motors, were recently added to Toyota's board of directors. Historically, Toyota's seven 'auditor directors' focused mainly on financial oversight and internal control issues. Thus, the decision to appoint three additional independent directors contributes to general expertise in the area of transparency, but also the business expertise that is likely to support the firm's global expansion plans and restoration of its brand as high quality car manufacturer. The decision can be explained in light of the analysts' decision to downgrade the economic moat from narrow to none after Toyota's recall crisis. In this case, there are two important lessons to be learned here: No matter what type of directors can be appointed (independent directors, non-executive directors, executive directors) and no matter who appoints the directors (minority shareholders, family members), the directors should always fit a certain profile designed to support (and monitor) the coordinator. The second lesson is that while balanced incentives are clearly needed directors should not be incentivized (by for instance bonuses paid by certain shareholders) to pursue an interest that may be destructive to the coordination with a company or group of companies (Masters 2014).

Figure 1: Six 'Material' Components of Corporate Governance



Finally, the role played by coordinator could also be a state or government. For example, the government is well entrenched in China Mobile that is owned and controlled by state-owned China Mobile Communications Corporation, which owns 74 percent. A former vice minister in charge of the telecom sector is currently the chairman. The coordinator role of the state, in terms of building a strong brand and a well-functioning strategy, is easily recognized and not disputed by the investors. However, there are costs to establishing a state as a coordinator. Beyond that, a common refrain for state-owned companies, such as China Mobile, is that it should pay more attention to investor relations. The combination of costs and the lack of transparency and the alleged corruption and bribery charges could disrupt coordination and hence the performance of the company. Certainly, these problems reinforce our discussion in Section two on the importance of disclosure rules and related party transactions for deterring all forms of self-dealing and opportunism. But it also demonstrates that it is critical that companies embrace an investor friendly strategy and communicate factors that help investors and other stakeholders assess the long-term potential and performance of companies. The fact that Chinese multinational in networking and telecommunications equipment, Huawei Technologies Co. Ltd, recently decided to disclose information about its ownership structure illustrates that some companies increasingly realize the importance of communication and conversation with investors (Sevastopulo 2014). In all cases, the major challenge for companies is that coordination systems are supported ideally by five other components: communication, conversation, connection, collaboration and co-creation. We will discuss the communication and conversation and the significance of investor relations strategies in the next Section.

2. Investor - Management Communication and Conversation

One aspect of the current debate on corporate governance is that it is vital for successful – and long-term oriented – companies to have engaged shareholders. It is therefore not surprising that policymakers and regulators increasingly introduce rules, regulations and best practices to stimulate the dialogue between a company's management and its shareholders. The regulatory provisions vary from the implementation of a stewardship code (which aims to enhance institutional investors' commitment and involvement in a company's strategy setting processes) to mandatory voting rules and more powerful shareholder rights at general meetings. If the sole focus is on the regulatory environment, this may lead to disappointing results because it does not assure that the investors' engagement will eventually lead to more growth and value creation. More importantly, the introduction of a regulatory environment could materially change current incentive patterns and perversely destabilize workable arrangements without assuring the appearance of more effective alternatives.

Indeed, investors already have adopted a wide range of engagement strategies, often dependent on their ownership stake in the company (Celik and Isaksson 2013). For instance, investors that own less than 2 percent usually employ a mix of active and reactive strategies. If the ownership lies between 1 and 2 percent, investors tend to become more active by using private and public means to convince the board of directors and management of necessary changes in strategy and organizational structure. Institutional investors with more than 10 percent of the outstanding shares are often represented on the board of directors in order to actively collaborate with management on the company's long-term strategy (Barton and Wiseman 2014). Rules and regulations (and usually also best practices) could also undermine the collaborative relationships and force investors to micro-manage and engage in risk-averse behavior. For instance, the implementation of rules that require mandatory voting on items of the agenda of the general shareholders' meeting forces investors (even if they have an insignificant stake) to also allocate resources and time to non-material and boilerplate agenda items.

Clearly, as we have seen, investor engagement is crucial to a well-functioning coordinator. The problem is that while policymakers and regulators have focused on allocating formal control rights in general meetings of shareholders, they often miss implementing provisions that are valuable (and often informal) in providing investors with more opportunities to interact with companies. Thus, companies (and investors) themselves can profitably embrace transparency and information sharing regarding growth expectations and strategies (Gapper 2014). Indeed, there are good reasons for a company to implement investor relations' strategies and establish a more frequent and timely dialogue with investors. Greater focus on making it easier for firms to disclose vital information to investors promises to result in better coordination of the branding and strategy dimensions of the firm. For example, attending investor conferences organized by the company itself or investment banks may help to stimulate more widespread interest in a firm. Investor conferences are generally attractive for companies seeking to generate trading volume and/or boost the stock price performance, but also to disseminate information about a company's organization and governance structure, which, if communicated well, could then be considered to be a competitive advantage for companies, thereby increasing the economic moat. This is another reason why the companies that are already world-leaders in their respective markets also attend investor conferences (see Table 4).

Furthermore, it is not just the mere interactions with investors, but the interactive discussion between executive management, investors and also the board of directors about the introduction of new products, product innovations and/or entering new markets that may prove to have a significant effect on the economic moat of companies (White 2013). We project three potential benefits for companies. First, the most important aspect of engagement may be connecting with leading institutional investors across the globe to explain and discuss growth strategies (and invite input). These discussions assist the coordinator in making better decisions and avoiding tunnel vision. Second, a similar focus is on identifying opportunities and getting a better sense of their peers and competitors that often attract the same investors. Third, (pro-) active engagement helps the coordinator in identifying expertise gaps on the board and executive teams (Goodman 2014).

Table 4: Investor Conferences/Meetings/Conference Calls in 2013

Company	Country	Investor Conferences
Apple	US	5
Walmart	US	14
General Electric	US	24
Microsoft	US	20
IBM	US	15
Nestle	Switzerland	15
Johnson & Johnson	US	10
Samsung Electronics	South Korea	25
China Mobile	Hong Kong	1
Google	US	7
Procter & Gamble	US	11
Pfizer	US	9
Roche	Switzerland	44
AT&T	US	18
Novartis	Switzerland	25
Coca-Cola	US	9
Toyota Motors	Japan	5
Anheuser Busch Inbev	Belgium	7
Oracle	US	14
Philip Morris	US	9

Source: FT Global 500 2013 (excluding oil and gas producers and financial institutions), Morningstar, Company Websites

It is noteworthy, however, that while investor-friendly companies are more likely to generate information about themselves for investors, there is no guarantee that investors actually appreciate the message. Consider Apple's Q1 FY 2014 Earnings Release in which it was announced that despite the excellent sales in foreign countries, 'headwinds' from foreign currency, particularly the Japanese Yen, had an adverse effect on the revenue growth. In terms of making information available to investors, the fact that Apple cited factors that are normally used by 'slow growth' companies was immediately construed by analysts that the firm's period of strong growth is over (McCahery and Vermeulen 2014b). Another example is Samsung's increased interaction with investors that was discussed in Section 2. During these meetings, Samsung arguably tended to overemphasize its dominant position in technology innovation. The problem with these over-the-top demonstrations is that they had little impact on their economic moat rating for two reasons. First, it is not entirely clear whether there is a market for the innovations. Second, it can only be expected that its competitors will accelerate efforts on these 'nice-to-have' innovations.

Prior research suggests that investor-management conversations are effective when the audience consists of professional or institutional investors. If the company's stock is predominantly owned and traded by retail investors, other investor relations' mechanisms can be helpfully employed. Family-owned luxury goods multinational LVMH Moët Hennessy Louis Vuitton S.A. is exemplary in this respect. It offers to minority retail investors, who own approximately 4.9 percent of the outstanding shares, the opportunity to become more involved by applying for a membership in their loyalty program, the Shareholders' Club. Another example of effectively targeting retail investors is

Walmart's Investor Relations App, which can be downloaded for free from its website. The App provides direct access to quarterly results, annual reports and global responsibility documents, but also, and more interestingly, financial news, international press releases and investor relations' activities. With such offers, the crucial question is what kind of other disclosures should be made to investors. Thus, the question is whether more detailed information should be provided about a company's strategy, innovation pipeline as well as the governance structure of subsidiaries and associated companies. This issue will be discussed in the next Section.

3. Connection, Collaboration and Co-Creation

There is little empirical research that has gauged the effect of collaborative and co-creation activities on deepening and widening the economic moat. To understand the formal and informal connections, collaborations and co-creation activities that can be truly material, we look at some examples of groups of companies to determine how these connections influence companies' sustainable growth and value creation potential.

One of the most important sources of innovation is a firm's partnership quality. For example, Johnson & Johnson's wide economic moat is arguably strengthened because it is viewed as a very attractive partner for biotechnology startups, which increases the possibility of Johnson & Johnson to bring new innovations to the market. In fact, the firm uses several techniques to establish a bigger window to the market of new innovations (connection). Consider its partnership with Index Ventures (a venture capital firm) and competitor GlaxoSmithKline. The €150 million fund targets single assets that have the potential to become leading products in the future, the so-called asset-centric investment model. The corporate investors provide advice to Index Ventures by appointing in-house experts on a scientific advisory committee. In order to avoid potential conflicts of interest, however, the two multinationals have not obtained any preferential rights (of first refusal) to promising drugs that could emerge from this partnership. If either party wishes to acquire an 'asset', they are required to engage in an open and competitive bidding process. Thus, Johnson & Johnson expects that its supportive partnership strategies will be beneficial in leading to the development of new drugs and medicines.

It would seem that General Electric (GE) also deserves part of its high economic moat rating because of the companies and divisions within the GE group that have significant synergies with other GE business units. GE's unique corporate culture enables these companies, divisions and units to support one another, which in turn lowers the operating costs and cost of capital (Hahn et al 2013). The connections and collaborations are also notable in research and development. An example is GE's new groundbreaking technology for jet engine fan blades that can also be used to GE's gas turbine engines. Another advantage of collaboration and co-creation is that sharing R&D costs makes it possible for GE to pursue projects that may be unprofitable for its competitors. The synergies and economies of scope that are an important component to GE's corporate culture cannot easily be replicated and thus gives the company a significant competitive advantage and wide economic moat.

The two above examples show how collaborations and co-creation activities within groups or multinationals can be truly material to companies' sustainable growth and value creation potential and useful for investors and analysts to make buy-sell decisions and recommendations about investments in these companies. The competitive advantages (economic moat) and the efficiency of capital allocations (stewardship grade rating) associated with a specific group or conglomerate structure – rather than responses to inefficient markets and underdeveloped legal environments (Granovetter 2005) – explain the current formation and development of corporate groups and conglomerates (Kuppuswamy and Villalonga 2010; Almeida and Kim 2012). On the other hand, critics tend to argue that these group and conglomerate structures may reduce the competitive advantage and may not always lead to significant benefits for investors (Carney et al 2011). Still it would seem, as indicated in this Section, that the success of corporate groups and conglomerates depends on how effective and constructive the coordination between the different internal and external parties is (Williamson 1985).

It appears that policymakers and regulators are also becoming aware of the fact that the crucial action in a company usually takes place at group and subsidiary level. Note, however, the question is whether policymakers and regulators should require companies to comply with specific rules and regulations concerning the structure and governance of a group/conglomerate. This becomes even more relevant in view of the European Commission's intention to introduce an initiative to improve both the information available on groups and the recognition of the 'group interest' as a legal concept (European Commission 2012). The rationale behind the regulatory initiative is that most legal systems around the world contain detailed sets of rules and regulations that govern separate legal entities, but largely ignore the group and conglomerate structures in which these entities operate (Gillooly 1993).

Indeed, it could be argued that this legal void, which is particularly present in international and cross-border settings, would open the door for opportunistic behavior within corporate groups and conglomerates. To see this, consider that a controlling parent company's interest is not necessarily aligned with the interest of the direct stakeholders (such as employees and creditors) of a subsidiary company. Presumably, the 'conflicts of interest' become more severe during reorganizations and downsizing. In order to avoid hold-up problems and create some level of legal certainty, the European Commission appears sympathetic to the group concerns. In fact, the Commission is currently contemplating the introduction of legal measures that safeguard and protects the 'group interest' (although it is also acknowledged that the interests of the subsidiaries' stakeholders should not be overlooked in the discussions) (European Commission 2011).

While the introduction of a 'group interest' may have some merit in theory, it may in practice have an adverse effect and even add to the (legal) uncertainty that surrounds corporate groups. For example, consider that the organization of groups and conglomerates are usually unique to each company, country and sector (Simmonds 1993; Zattoni 1999). Moreover, academic research indicates that the design and structure of a group of companies is usually the result of a mix of conscious strategic and financial planning without disregarding complex legal, regulatory and tax considerations (Rasmussen 2002; Harris and Hargovan 2010). Thus, it appears that it is extremely complicated to define and constitute a 'group interest'. This is particularly true in groups with apparently unrelated or distantly related businesses.

Similarly, corporate groups and conglomerates may not only consist of wholly owned subsidiaries and other associated companies (including listed subsidiaries), but are often also structured through contractual forms, including franchise arrangements and licenses (Blumberg 2013; Eisenberg 1993). A major concern is that the complexity of legally defining and protecting specific group interests is exacerbated if the coordination, organization and management of groups and conglomerates cannot be captured through straightforward concepts of corporate governance and company law. For instance, it should be noted that coordination and control in international conglomerates is not always determined by company law relationships that exist between a parent company and its associated companies. This is reinforced by evidence that shows that it is difficult to find the right balance between shareholder and creditor protections, the recognition of a group interest, anti-trust policies and the desire of companies to pursue growth and value creation through a group or conglomerate structure (Belenzon et al 2012).

The argument that more accurate information about the structures of a corporate group or conglomerate would help investors making better investment decisions is also not convincing. Surely, companies can make information available about the coordination, management and organization of their groups. In fact, related party transaction rules and accounting rules on consolidation already ensure that investors and other stakeholders receive group information in a company's annual account. However, there is very little gain implementing more detailed rules and regulations that will most likely lead to generic and boilerplate statements that are largely non-material to investors and other stakeholders. As noted above, it is preferable if both the companies and their investors focus on metrics and information that are material to their growth potential and competitive position. Hence, we predict that the connections, collaborations and co-creation activities will emerge as a leading edge item on the agenda of the investor-management meetings and conversations. There is little evidence, however, that the introduction of 'group law' will lead to revenue enhancement and efficiency gains in the long run. On the other hand, the value of developing new strategies on how to contribute to a culture that fosters valuable communications and conversations between a company's management and board of directors and its investors is likely to have real effects and would serve as the basis for an alternative policy perspective on groups of companies.

III. Conclusion

In this paper, we have presented a model of corporate governance that arguably plays an important role in enhancing sustainable growth and value creation in companies. This new model helps identify and distinguish the truly material corporate governance rules and norms from the non-material ones by analyzing their impact on the economic moat, uncertainty levels and stewardship grade ratings.

The model revolves around six key components. The first, and most important component is coordination. There is no such thing as a successful company without coordination. The logic of coordination is that it provides a link between the investor community, the business divisions or business units and the customers or society. However, a sole focus on coordination is not sufficient. We have shown that communication and conversation with investors are also important components at the headquarters' level. The group (subsidiary) level coordination is supported by three other components: connection, collaboration and co-creation. Companies that have embraced the six components are usually wealthier, healthier and more competitive. Despite the different patterns of ownership and control, we show that companies have found different ways to give substance to these six components. Our analysis indicates that firms with different forms of ownership, such as family-controlled companies, are also able to embrace the six components effectively. A major conclusion to be drawn form our study is that firms will continue to encounter difficulties if the deviations from what is generally accepted to be good corporate governance are not recognized as a key source of a company's culture and competitiveness.

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