Business studies

Understanding corporate ownership types

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Introduction

The structure that determines organisational ownership is intrinsically linked to the process of corporate governance. It is the capital ownership configuration that will have the most influence on the structure of the board, the future performance of the firm and ultimately determine where its strategic control is focused. Essentially, therefore, as argued in the literature (Mayers et al 1997; Marchica and Mura 2005), control of the business will be dependent on the trade-off between ownership type and board composition.

Following a brief review of the historical development of corporate ownership structures, this essay will examine theses within the context of UK corporations. For this purpose, two diverse ownership corporations will be used for analysis purposes. These consist of John Lewis PLC (Managerial ownership), and Marks and Spencer PLC (Shareholder ownership).

The development of diverse corporate ownership structures

Prior to the early part of the twentieth century, there was limited corporate investor protection. This meant that managers and board directors could easily discard the needs of investors in favour of their own interests (Marchia and Mura 2005), a situation which tended to deter external investment. However, in the later part of the 1900s and the early 2000s, following increasing concern over the adverse consequences of board decision-making, there has been a plethora of changes to company law, and the introduction of corporate governance regulations aimed at addressing this situation and improving investor protection (Cheffin 2008).

The consequence of these changes has led to an expansion of external share ownership, predominately through public stock exchange listing as well as a change in capital structure and board composition. In terms of corporate control, both of these latter elements are interrelated. In this context it follows that the larger the shareholding, the greater will be the influence that investors can exert over board appointments. This has resulted in an increase in the numbers of non-executive directors being appointed, whose task is solely to ensure management decisions reflect the interests of the external shareholders (Cheffin 2008).

Table 1 provides an example of how the capital structure of UK listed corporations changed during the decade to 2001.

Table 1 Changes in corporate capital structure 1991-2001

Average percentage of ordinary shares held by outsiders and insiders												
		1991*	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Block holding		20.72	31.61	33.21	29.11	29.87	31.09	32.39	33.13	33.80	33.40	32.43
Institutional Ownership		12.63	22.31	23.22	20.52	20.96	22.84	23.38	24.51	24.52	24.00	22.30
Non-institutional Ownership		8.10	9.30	9.99	8.59	8.90	8.25	9.01	8.62	9.28	9.40	10.13
Largest non-managerial		8.53	9.10	9.67	10.03	10.32	10.78	11.01	11.42	11.00	11.83	11.45
Board Ownership		15.26	13.71	13.13	11.88	12.24	10.99	10.80	10.28	10.51	10.19	10.70
	Executive Directors	13.34	11.93	11.30	9.97	9.94	8.94	8.54	8.16	8.15	7.43	7.61
	Non-Executives	1.92	1.77	1.83	1.90	2.29	2.06	2.26	2.11	2.36	2.76	3.09
	Float	64.02	54.69	53.66	59.01	57.90	57.92	56.81	56.59	55.69	56.41	56.87
Total sample firms		565	583	611	645	666	667	661	606	501	440	395
Average number of outstanding shares (in millions)		145	154	165	174	203	185	184	314	247	290	288

* Reported disclosure rule is 5%
Block holding represents the average shareholding by external shareholders who own at least 5% of the shares
Ownership by Institutions is the sum of the shareholding of financial firms.
Ownership by non-institutions is the sum of shareholding by private individuals and other non-financial firms.
Board Ownership represents the average shareholding by managers as either "Executive" or "Non-Executive" Directors, including Chairman and Chief Executive Officer.
Float is the average percentage of shares being held under the disclosure threshold of 3% except for 1991

Source: Marchica and Mura (2005)

It is clear from this example that the percentage of external shareholding, as represented by the first four items listed, has changed significantly during this observational period, with block holdings increasing by just over 50%. At the same time, the level of board ownership has decreased by around a third. It is therefore perhaps not surprising to find that this event has had an impact on the composition and size of corporate boards. As indicated in table two, while the average number of board members has seen little change, there has been a significant move towards equalisation, both in terms of the relationship between executive and non-executive directors and their respective shareholdings.

Table 2 Change in board composition and size

Board Size and Board Composition												
		1991*	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Total Board Size		7.13	7.13	7.18	7.17	7.33	7.32	7.28	7.33	7.38	7.39	7.35
	Executive Directors	4.73	4.59	4.44	4.31	4.24	4.15	4.05	4.00	3.94	3.92	3.82
	Non-Executive Directo	2.44	2.54	2.74	2.86	3.10	3.18	3.23	3.32	3.44	3.47	3.53
Proportion of Non-Executives to Total Board		0.34	0.36	0.38	0.40	0.42	0.43	0.44	0.45	0.47	0.47	0.48
Executive Directors cum-shares		4.04	3.91	3.81	3.68	3.69	3.60	3.55	3.56	3.50	3.47	3.39
Non-Exec Directors cum-shares		1.90	1.92	2.02	2.13	2.37	2.47	2.49	2.64	2.73	2.78	2.81

This table shows the average number of members on the Board of Directors. Executive Directors here include Chief Executive Officer and Executive Chairman and Non-executives include the Chairman. Executives and Non-Executives cum-shares are those who effectively own shares in the company.

Source: Marchica and Mura (2005)

These statistics serve to confirm that the control of the corporation and its performance is becoming more heavily influenced by external shareholders and their board representatives (Non-executive), and thus reducing the decision making influence of the executive board.

Nonetheless, there remain other forms of UK corporate ownership where internal shareholders can also have an influencing effect on board decision-making. Predominantly these are likely to consist of mutual ownership, a structure most commonly associated with building societies and some insurance companies, and managerial ownership (Cheffin 2008). In the latter case, usually associated with privately owned corporations, individuals directly involved with the business, including managers and employees, tend to be shareholders and represented on the board. The benefit of managerial ownership is that control remains firmly in the power of employee/managers and the firm can remain resistant to outside influences (Mayer et al 1997). As noted previously, the UK public corporate environment now mainly comprises of firms exhibiting a dominance of external or outside shareholders, commonly denoted as dispersed ownership" (Marchia and Mura 2005). By their very nature, it is uncommon for firms with managerial ownership to be listed. However, the John Lewis Partnership is an exception to this rule, and therefore from the point of view of corporate control and influence provides an ideal firm to use for comparison purposes.

Comparing the ownership structure and influence at John Lewis PLC and Marks & Spencer PLC

Marks and Spencer PLC, and John Lewis PLC represent two different types of listed firms in terms of their ownership structure and board composition. This differential has a significant impact on the influencing factors on the control of the firm and its performance. Table 3 on the following page provides relevant comparatives for the two firms, using data that has been presented in their respective annual reports for 2012 and 2013. Table 4 then provides a breakdown of the board composition and an outline of the type of employee influence.

Table 3 Capital structure

John Lewis Partnership PLC	2013	2012
Share Capital	6,750,000	6,750,000
Total holdings	6,750,000	6,750,000
Held by internal Individuals	100.0%	100.0%
Held by external Institutions and individuals	0%	0%
Management and employees (Partners)	1 share each	1 share each
Profit/(Loss) pre exceptional items	£449,700,000	£391,000,000
M&S PLC	**2013**	**2012**
Capital	403,500,000	401,400,000
Individuals	100%	5.36%
Held by external Institutions and individuals	0%	95.59%
Management	1 share each	0.05%
Profit/(Loss) pre exceptional items	£458,000,000	£489,300,000

Table 4 Directors

Director Type	John Lewis	M & S plc
Total	15	14
Executive	12	6
Non-Executive	3	8
Influence of employees	1 share each and a democratic council which elects and advises the board	There is a share scheme but the employees have no direct influence over board decisions

Sources: John Lewis Plc (2013) and Marks & Spencer (2013)

As noted in these tables, the total capital of John Lewis Plc is totally owned by the employee (partners) employed in the business. Moreover, it is these employees who, through their ‘partner council’, who elect the majority of the board executive directors and appoint a counsellor to the board (Editorial 2007). It follows that the employees have a significant influence of board-decision making and the performance of the firm. Furthermore, a reasonable percentage of the corporate profits are shared with the workforce based on a percentage of their earnings (17.4% in 2013) (John Lewis 2013).

In contrast, it is apparent that the employees and board members of M&S hold a minute percentage of the firm’s capital. The percentage of capital owned by external institutions and individuals gives these groups a greater say and influence over firm performance and the actions of the directors (Cheffin 2008). This control is apparent from the fact that the numbers of non-executive directors on the board of M&S, who act as shareholder representatives, exceeds that of executive directors (Liu and Sun 2005). This structure also means that through the non-executive members of the board the external owners of M&S are able to monitor the performance of the main board and its impact on shareholder interests as well as corporate objectives more closely.

Conclusion

It follows from the preceding discussion that the John Lewis board is not subjected to market influences or their demands for continual matching profitability expectations in the same way as M&S. Instead, it is driven and influenced by the objectives and demands of the management and employees, whereas the M&S board is heavily influenced by external forces and owners. Therefore, as Liu and Sun (2005) rightly indicates the ownership class of a corporation is likely to determine whether influence and control is located in external or internal forces. However, one commonality that is shared by both structures is that, irrespective of whether the influences are internally or externally driven, is that both serve to limit the potential for executive directors to make decisions based on their own self-interests rather than those of owners (Liu and Sun 2007).

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