Corporate Governance and Human Resource Management

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Abstract

In seeking to compare the consequences of different corporate governance regimes around the world, an initial focus was on overall growth consequences. However, given that different types of national corporate governance regime appear to do better than others at specific times, and the great variations in national development within the main broad national corporate governance families, there has been a growing interest in the specific effects on the firm itself [Morgan et al., 2010], rather than seeing it as a transmission belt between relative owner and stakeholder rights on the one hand, and macro-economic outcomes on the other hand [La Porta et al., 1997, 1999, 2000]. At the simplest, such analysis has sought to interpose relative worker rights and social protection under the law as a variable that might dilute owner rights, diverting firms from a shareholder value maximisation agenda [Botero et al., 2004]. However, this goes little beyond simple hierarchical models that suggest that a single institutional feature underwriting property rights can explain everything of significance that goes on in the firm. So a growing body of applied work looks at the consequences of dominant corporate governance regimes for a key stakeholder grouping that has sunk human capital within the firm. Indeed, arguments are made for a re-evaluation of types of institutional arrangement and associated patterns of firm finance in relation to what might best explain particular sets of HRM and employment practices, and the direct effect on organisational performance, alongside how this might affect overall economic growth [Goergen et al., 2012, Gospel and Pendleton, 2003, Black et al., 2008, Pendleton, 2005]. There are many different dimensions to national corporate governance regimes, encompassing the legal, the political, the economic, and, indeed, embedded patterns of social behaviour; there is much debate within the literature as to which is the most important aspect of each.
1

Different Traditions of Comparative Institutional Analysis: Owner and Worker Rights

1.1 Rational Hierarchical Accounts

There is a wide body of literature on the effects of institutions on firm practices [Morgan and Kristensen, 2006, Lane and Wood, 2009, Lane and Probert, 2007]. However, within the corporate governance tradition, there are two dominant strands: rational hierarchical approaches that are founded in the orthodox economic tradition, and heterodox socio-economic alternatives. However, what is particularly confusing is that quite a body of the existing literature treats different institutional approaches as somehow interchangeable, sometimes including the quite different sociological approaches of writers such as Scott [1988] into the general mix. Traditional economic accounts have been termed ‘rational–hierarchical’ in that they assume that institutions incentivise or disincentives rational actors, whilst a single institutional feature dominates all others [North, 1990, 1994, 2006].

The foundation of orthodox economic approaches lies in Douglass North’s [1990] influential 1990 account, where he argued that the institutional foundations of private property rights could explain the very distinct economic fortunes of nations. Following this, La Porta et al. [1999, 2002] suggested that the foundation of private property rights
1.1. **Rational Hierarchical Accounts**

lay in legal origin. They identified two ideal type regimes: common law and civil law. As common law countries were associated with stronger private property rights, they would inevitably perform better, and they backed up their argument with economic evidence from a range of countries, concentrating on the 1990s. They subsequently extended their analysis, by looking at the effects of employee rights and social protection. Not only were the latter also bound up with legal origin, but also they inevitably diluted owner rights, making for worse economic performance in civil law countries [Botero et al., 2004]. This approach has been hugely influential with the policy community, most notably via the World Bank *Doing Business* reports [Cooney et al., 2010, Michaels, 2009]; undeterred by the fact that it is not easy to change legal origin, the latter body has aggressively pushed to deregulate labour markets, on the assumption that such interventions will leave property owners better off, and this will be good for growth. The argument is that what happens in organisations is that managers are thus forced to align with the interests of owners, rather than conspiring with workers in *empire building* projects that maximise employment in the interests of prestige (2006). So managers will use flexible and contingent employment, allowing the firm to adjust rapidly to external challenges, with skills being secured on the external labour market. The absence of collective worker rights reduces the chance of the emergence of coherent interest groupings in the workplace, allowing owners to develop forms of incentives that reward maximum individual effort [Botero et al., 2004]. Hence, strong owner rights and weak countervailing worker power are likely to contribute to resolving agency problems, and aligning the firm more closely to the dominant agenda of owners (ibid.).

At the broadest level, this approach has attracted a range of critiques, many of which have focused on the relationship between owner rights and those of workers. Firstly, it has been argued that the empirical foundation of this approach is conveniently founded on periods when common law countries were performing particularly well, and an analysis of earlier decades would have yielded very different results [Wood, 2011]. Secondly, within common law countries, key dimensions of corporate law, most notably surrounding bankruptcy, have arisen from
Different Traditions of Comparative Institutional Analysis

legislation, rather than judicial decisions; quite simply, legal traditions are complex, and there is always an element of uncertainty to how laws evolve [Davis and Kruse, 2007]: there is a tendency for innovation in the development of corporate law [Pistor et al., 2003]. The same goes for key dimensions of labour legislation, such as the minimum wage in the United Kingdom [Deakin et al., 2007]. Indeed, it has been argued that labour law has evolved in different countries in a manner that is quite removed from legal origin [Deakin et al., 2007]. We might add that the influence of the European Union has meant that similar employment legislation has been introduced in all the 28 member states even though, on the La Porta et al. analysis, they have very different legal origins. Further, it has been argued that the development of legal cultures within different countries creates distinct effects in each, whilst the relative timing of industrialisation appears to have had a greater effect than legal origin per se [Ahlering and Deakin, 2007]. Other work has pointed to the distinct effects of state enforcement capabilities [Almeida and Carneiro, 2009]. It has been argued that different types of labour regulation have different effects and that, in labour intensive industries, employment protection laws exert relatively strong effects whilst, in capital intensive ones, dispute resolution procedures become more important. This would reflect variations in the relative cost and bargaining power of labour [Ahsan and Pagés, 2009].

From within the broad sociological tradition, Emile Durkheim’s [1957, 1969] classic writings also accorded a central importance to the law in economic life, but argued that economy and society were inexorably interlinked. Hence, the problem was not so much the relative security that private property owners could enjoy, but the challenge of reconciling individual interest with maintaining the degree of collective cooperation that characterises the modern workplace, and indeed, social life (ibid.). In other words, rather than collective rights necessarily undermining the individual rights necessary to protect private property, the potential of the latter can only be realised with a degree of collective cooperation that can be secured and upheld through rights
1.1. *Rational Hierarchical Accounts*

under the law [Cotterrell, 1999]. This would suggest that there is not an inverse relationship between individual and stakeholder rights.

La Porta et al. [1999] seek to categorise all economies on a scale from strong property rights on one pole to strong stakeholder rights on the other pole. In practical terms, La Porta et al. [1999] suggest that, in addition to pure common or civil law, German and, to an even greater extent, Scandinavian civil law, represent diluted versions of civil law, incorporating elements of common law. This would account for the better performance of these economies than pure civil law ones. This would suggest that there is somehow a fixed amount of rights to be ‘divvied out’, whilst a Durkheimian approach would argue that legal systems confer variable elements of both formative historical experiences and the ongoing need to mediate economic activity, and it is possible for owners or stakeholders rights to be increased without the others' rights necessarily decreasing [Cotterrell, 1999, Lukes and Scull, 1983, Sutton, 2000].

However, comparative empirical analysis of firm level HRM [Brewster et al., 2015a,b,c] suggests that Scandinavian civil law is not simply a stage on the path to common law. Rather, based on the Cranet surveys of HRM practice, it appears that workers in Scandinavia enjoy stronger and more effective collective representation at the workplace than typically encountered in pure French civil law systems. The same is true, to a lesser extent, in German civil law countries. In other words, even if La Porta’s assumptions as to owner rights in Scandinavia are correct, their view that this will be associated with weaker worker rights is demonstrably false and/or we must accept the view that worker rights do not necessarily dilute owner rights [Wood, 2011]; owner and worker rights are not a zero-sum game. This would suggest that even if there are fundamental differences between common and civil law countries, national institutional environments cannot necessarily be placed on a linear scale between ideal archetypes. Rather, as suggested by Durkheim, the complexities of modern organisational life necessitate greater or lesser compromises both in law and practice.

\footnote{Indeed, in the Nordic countries, as the evidence includes Finland — here, for simplicity, we adopt the terminology used by La Porta et al.}
Different Traditions of Comparative Institutional Analysis

and different systems may arrive at them through mixing and hybridising different elements of regulation [Brewster et al., 2015a,b,c, Sutton, 2000]. This does not mean that, in many national contexts, growing numbers of workers might not find themselves in a highly precarious position, with contingent employment contracts; rather, such trends represent the breakdown of more complex forms of mediation with uncertain consequences [c.f. Kalleberg, 2009].

At a more applied level, the assumption that strong owner and weaker worker rights make a more attractive investment environment has also been contested, the confidence with which such policy prescriptions are promoted notwithstanding. For example, Wood et al. [2015] investigate FDI flows into South Eastern Europe, a region characterised by quite ambitious reforms to both corporate law and labour markets. They found no connection between the relative extent of labour market deregulation and the relative attractiveness of a country to foreign investors; indeed, quite regulated contexts such as Slovenia were notably successful in attracting FDI. This would reflect the complex competitive advantages conferred by sets of national level institutions; firms opt to invest in countries in order to benefit from a particular national production regime which may or may not be associated with stronger property owner and weaker worker rights (ibid.). Again, regulatory reforms may hold little or no benefit for key groupings, most notably small and micro-enterprises [Lyons and Msoka, 2010].

A variation of property rights centred approaches looks at the effects of national electoral systems. What is broadly argued here is that ‘first past the post’ majoritarian electoral systems are likely to favour the rights of property owners over proportional representation ones [Pagano and Volpin, 2001, 2005, 2006]. The reason is that within the former, elections are likely to be decided by ideologically uncommitted swing voters; in the latter, there is a greater likelihood of coalition governments encompassing a range of different interest groupings (ibid.). There is some broad evidence to support the effects of electoral systems; liberal markets tend to be first past the post, and more coordinated markets proportional. However, there is little link between electoral system and national development within the mature democracies; there
1.1. Rational Hierarchical Accounts

are very wealthy countries that fall into either category. In the developing world, it seems that there is a greater variation in property owner rights according to the relative powers of the presidency than electoral system *per se* [Brunnschweiler and Bulte, 2008]. Again, there seems to be divergence in corporate governance and worker representation between Germany and Scandinavia, despite the presence of proportional representation in both countries [Goergen et al., 2009a, Jackson, 2005]. And, there are important exceptions to the general rule. Ireland has a proportional electoral system, but has generally followed a liberal market trajectory, the neo-corporatist experiments of the 1990s and early 2000s notwithstanding [Fraser et al., 2013]. Again, successive Estonian governments have tended to favour neoliberal policies, despite a proportional representation electoral system [Bohle and Greskovits, 2007]. This was facilitated by the fact that many of the poorest voters, ethnic Russians who had the most to lose by such reforms, encountered great difficulties in being able to vote on account of strict nationality laws [Hughes, 2005], even if later these rules were somewhat reformed. In other words, neoliberal policies may be facilitated by specific sets of historical circumstances that may have little to do with electoral system *per se*. Finally, despite changes in the electoral system, there are long continuities in Japanese government policies, with many of the core defining features of more coordinated markets, including embedded consultative and long term human resource development mechanisms in Japanese firms [Thelen and Kume, 2006, Horiuchi and Saito, 2003, Vogel, 2001].

It could be argued that moneyed interests are more powerful in first past the post systems, as concentrating political party funding in areas where the above mentioned ideologically uncommitted swing voters are concentrated may help decide the election [Herrera et al., 2008]. Again, the ample opportunities for gerrymandering in the United States and the United Kingdom make it easier to weaken the voting power those sections of the electorate most marginalised by a present order [Johnston, 2002, 2015]. Moreover, it could be argued that it is not owner interests *per se* that necessarily win out in such circumstances; rather it is those segments of capital most willing and able
to devote resources to political party funding, and to support individual politicians most malleable to their will [Farrar-Myers and Skinner, 2012, Kang, 2013]. This would include those in industries most dependent on state largesse, those that are reliant on light regulation (e.g. very polluting industries and segments of the food and beverage industries) and individuals with significant amounts of uncommitted capital at their disposal [Lundskow, 2012, Formisano, 2012]. This would suggest that such systems are not necessarily benign in their effects on other categories of investor less reliant on state largesse or lack of oversight. In such circumstances, rather than still being able to count on the trickle down effects of generally rising national prosperity, workers may face long term political marginalisation and a further erosion of what accrues to them [Talbott, 2011].

1.2 Developments and extensions of rational hierarchical accounts: Property owner rights and workers — the case of Africa

The panel of countries encompassed in La Porta et al.’s analysis, and similar accounts, must be open to question. Conveniently, the analysis includes the largely civil law West African states, which have had chronic developmental problems largely unrelated to legal origin. This would range from the historical legacies of slavery to the high incidence of a large number of tropical diseases. Indeed, other accounts from the broad property rights tradition, have argued that there were some quite different structural causes for the poor growth in the region that transcend legal origin. This would include Herbst [2014], who suggested that the relative availability of land in Africa led to labour becoming a more prized commodity during colonisation; this left a tradition of weak property rights and labour coercion, and artificially created states that were divorced from the pre-colonial past. Others, such as Acemoglu and Robinson [2006] pointed to the very different developmental experiences of societies with large concentrations of settlers with those that did not; this makes it difficult to reach conclusions as to relative development based on legal origin alone. In the colonial era, in
1.2. Developments and extensions of rational hierarchical accounts

territories that did not attract significant numbers of settlers, attention was focused on coercive institutions and expropriation, whilst in those that did so, much more effort was devoted to replicating the constitutional arrangements of the metropole [Herbst, 2014, Acemoglu et al., 2000]. However, these approaches are rather ‘broad brush’, and accord little attention to the effects of dominant modes of corporate governance on labour and HRM within the firm.

Recent work by Wood et al. [2013] has suggested that autocratic management and the weak position of employees within the firm in Africa reflects a specific institutional tradition, associated with very uneven and volatile economic development, meaning that regular employment is the exception rather than the rule for job-seekers. At the same time, the effects of autocratic management are somewhat alleviated through informal extended networks of support, with the families of existing employees being favoured in recruitment and with informal cash loans supplementing low pay [Webster and Wood, 2005, Wood et al., 2011]. Finally, in many settler orientated colonies, parallel security states were established to facilitate labour repression and the expropriation of indigenous land holdings; where these have persisted into independence, these have facilitated the suppression or emasculation of labour movements.

What these accounts tell us is that owner rights may represent the product of complex historical legacies, and that specific institutional features cannot be understood separately from their setting. This would suggest that, even if countries may be of common or civil law legal origin, the circumstances under which such law was established, internal regulatory coherence, and the effects of competing state structures, may yield very different outcomes to those anticipated [Mamdani, 1996, c.f. Joireman, 2001]; within Africa, it is most commonly the case that there are at the same time both weaker owner rights and weaker de facto worker rights when compared to developed common law states. This is not simply about limitations in state capabilities — although any shortfalls in this regard are likely to be non-trivial — but also about the relative coordination of different arms of government, and
the potential for each to follow quite different trajectories [c.f. Herbst, 2012].

Again, civil law countries in Africa differ greatly in terms of the policies of the metropole. The colonial experience in much of Francophone Africa was relatively short, and this was associated with the development of institutional arrangements that proved relatively fragile, regardless of variations in legislation [Blanton et al., 2001, Mammadani, 1996]; however, it should also be considered that the Francophone colonies were concentrated in West Africa, an area with a high incidence of tropical diseases, posing serious developmental challenges regardless of regulation [Sachs, 2001].

Unlike most European powers, whose role, in most instances, lasted less than a century, the Portuguese retained a presence in Africa for almost 500 years. The Portuguese colonies shifted from a rule by agents (prazedios or feudal warlords, succeeded by chartered companies) to direct rule under the fascist Estado Novo [Newitt, 1973, Newitt and Rothman, 1981]. The latter was characterised by attempts to settle large numbers of Portuguese peasants and to mirror the institutional arrangements of the metropole. However, the Portuguese state was very weak and under-resourced, and these efforts were, at the best, only partially successful. Wearied of endless colonial wars, the 1974 Revolution of the Carnations led to the end of fascist rule in Portugal and immediate decolonisation [Harsgor, 1980]. Many settlers fled and the incoming revolutionary governments experimented with state socialism [Rocha-Trindade, 1995, Sidaway and Simon, 1993, Scott, 1988]; in the case of Mozambique and Angola, this was followed on by civil conflicts, with the rise of rebel movements nurtured and sponsored by apartheid South Africa and the CIA. The end of the cold war led to the end of such conflicts, and democratisation in all the former Portuguese colonies, accompanied by radical neoliberal reforms [Wood and Haines, 1998, Wood, 1999]. However, a remarkable feature was that, despite all these systemic shocks, there was continuity in firm level HRM practices, largely following on the autocratic paternalist model outlined earlier [Webster et al., 2006, Wood, 2011].
1.2. Developments and extensions of rational hierarchical accounts

What does this tell us about institutions and corporate governance? The first implication is that there is a great deal of difference between formal and informal modes of regulation, so that all manner of radical reforms in corporate law (and, indeed, formal macro-economic policy) may have only limited effects on what managers actually do. Faced with policy turmoil, managers seem to have responded by sticking with the tried and trusted tools and techniques of the past, coping with changes through informally negotiated understandings and concessions [Webster and Wood, 2005, Webster et al., 2006]. The second is that informal sources of firm finance may, in some contexts, underpin a large proportion of firms. In the case of Lusophone Africa, this has taken the form of many small businesses being interlinked through extended family networks back to small entrepreneurs in the former colonial metropole, Portugal [c.f. Wood, 1999, Menzies, 2000, Benzing and Chu, 2009]; whilst not constituting formally structured multinational enterprises (MNEs), such networks have provided many small players with capital, equipment and skills.

However, the distinct features of different colonial experiences should not blind us to certain commonalities in institutions and in firm practice in developing economies around the world. Even if not on the extended trans-national lines encountered in Lusophone Africa, many developing economies are characterised by the dominant role played by family owned businesses, who are adept at navigating institutional arrangements of uneven functionality or spread [see Tabalujan, 2002]. Rather than focusing on the formalities of corporate law — or worker rights, the relationship between corporate governance and HRM represents a product of what type of solutions such firms are able to arrive at through combining formal and informal regulatory arrangements [Wood et al., 2001; Wood and Frynas, 2006]. Whilst the resultant HRM systems are unlikely to conform to the advanced models encountered in the West (either in common or civil law countries), they will allow some basis for organisational stability and growth, even if the outcomes for investors and workers are sub-optimal.
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