



Corporate Governance in Contention

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Foundation Ownership and Firm Performance

A Review of the International Evidence

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Abstract and Keywords

Foundation ownership of business companies is a governance structure which combines philanthropy and business. It is common in Northern Europe, particularly in Denmark. This chapter explains the basic governance structure, including the role of the foundation boards and company boards in foundation-owned companies, as well as the role of foundation law, government supervision and capital markets. It goes on to review the international evidence on the performance of foundation-owned companies, drawing on academic research from Scandinavia, the Netherlands, Germany, Italy and the US. The evidence indicates that foundation ownership is a financially sustainable and socially responsive governance model, which could be more widely used around the world. However, successful foundation ownership requires a climate of good governance that cannot be taken for granted.

Keywords: Industrial foundations, corporate governance, CSR, company performance, profitability

4.1 Overview

In this chapter, we review what is known about the economic performance of foundation-owned companies. We build on the evidence in a recent book (Thomsen, 2017), to which we refer for documentation and details. There is evidence that foundation ownership has attractive social functions. For example, foundation-owned companies tend to be responsible employers, who pay their employees well and fire them less often (Børsting and Thomsen, 2017).

Moreover, foundations take a long-term perspective on their businesses, which contrasts favourably with contemporary discussions of short-termism in investor-owned companies. Empirical research indicates that foundation-owned companies are in fact more long-term than conventional business companies (Børsting et al., 2016). They replace managers and board members less often. They are more research-intensive. They have more stable earnings and less leveraged balance sheets. They survive longer.

Despite all of these apparent advantages, foundation-owned companies may also be subject to governance weaknesses, which could reduce their efficiency and business relevance. For example, the diminution of profit motive may imply insufficient attention to cost efficiency. The foundations may be reluctant to dilute their control, making it more difficult to attract outside equity. They lack a market for corporate control to remove inefficient executives. Sceptics would claim that these weaknesses cast doubt on the financial viability of foundation ownership.

Foundation ownership seems to be an example of a different kind of private enterprise that is not subject to the shortcomings of financialization. Foundation ownership also seems to avoid the problems of succession, family conflicts, and **(p.67)** nepotism which plague family businesses. Moreover, foundations are private entities that are not subject to the familiar problems of state-owned enterprises, such as political interference or soft budget constraints.

What makes foundation ownership particularly interesting to corporate governance research is that it combines charity (foundations) with business (ownership of a business company). Foundations must serve a non-selfish purpose like charity, and as such, they are socially responsible by design. What is new to an Anglo-American audience is that regulators in Northern Europe consider ownership of a company to serve a useful social goal.

In this chapter, we try to assess whether foundation ownership is viable by reviewing previous academic research on the relationship between foundation ownership and firm performance, by which we mainly mean firm profitability, although it is far from obvious that firm performance should exclusively be measured by profitability.

Industrial foundations are found around the world, but nowhere as frequently as in Denmark. They are a rarity in the US and UK. In a few countries (Denmark, Germany, Sweden) empirical academic studies exist, but in the rest of the world, we have to rely mainly on case studies and legal scholarship. The review is structured by country, starting with Denmark. It goes on to discuss Sweden, Germany, Austria, the Netherlands, Italy, the UK, the USA, and a number of other countries.

We conclude that foundation ownership is financially viable in the sense that the financial results of foundation-owned companies are comparable to those of other private companies. Therefore, we argue that regulators around the world should encourage the formation of industrial foundations, and at the very least not block them with artificial legal constraints.

4.2 What are Industrial Foundations?¹

Industrial foundations are foundations that own business companies. Typically, the foundations are established by entrepreneurs wishing to secure the future of the company. Therefore, the founders establish a foundation and donate their company stock to it.

We prefer the term ‘industrial foundations’ instead of ‘commercial foundations’, since the foundations do not serve a commercial purpose. They are not means to profit maximization, but accountable to their charters and regulators.

Foundations do not have residual claimants or a profit motive. Alternative terms used in the literature are ‘corporate foundations’ or ‘enterprise foundations’.

(p.68) The donation is irrevocable. After formation, foundations are governed by a foundation board (equivalent to a UK board of trustees), whose fiduciary duty is to the foundation and the goals expressed in its charter. The principal assets of the foundation are shares in the company, from which they receive dividends. Most combine a business goal (preservation and development of the company) with a philanthropic goal, which is funded by dividends from the company. Typical goals would be support for research, education, art, or social projects.

Foundation governance varies considerably. In some cases, the foundation board and the company board overlap completely (i.e. they consist of the same people). In other cases, the two boards are completely separate. Formally, the foundation board governs the foundation, for example its donations or portfolio allocation, while the company board is in charge of the company. However, foundations are more or less active owners. At a minimum, they are expected to appoint the board members (in co-operation with minority investors) and to ratify major decisions regarding M&A and capital issues. However, typically they want to be able to sign off on overall business strategy and the appointment of the CEO. Furthermore, they will be regularly briefed on the financial situation of the company and other important issues.

The foundation board is typically self-elected (self-perpetuating), but in some cases foundation board members are appointed by outside parties such as the founding family, the Danish Royal Academy of Arts and Sciences, or (formerly) by the Ministry of Justice. While this may seem to be problematic from a governance viewpoint, empirical research has detected no performance differences between foundations with self-elected board members and board

members appointed from outside. If anything, the self-appointed boards appear to do better, financially (Thomsen, 2017: chapter 9).

Danish industrial foundations are regulated by the Foundation Authority—a government agency under the Ministry of Business. The Foundation Authority exercises legality supervision, which is limited to ensuring that foundations comply with the law and with their foundation charter (which is written by the founder and approved by the Foundation Authority). Thus, the Foundation Authority cannot intervene in business decisions. The foundation owners can request any kind of information from the foundations and even appoint an outside auditor or lawyer to scrutinize the company. Moreover, the regulators have to approve changes to the charter and extraordinary business decisions, which might jeopardize foundation's ability to fulfil its stated purpose(s). The Foundation Authority has wide-ranging powers, for example to replace the board, but this happens rarely in practice. However, it intervenes once in a while, for example in donation policies or board member compensation.

Foundation-owned companies can raise capital in the same ways as other companies, but foundations will often want to secure voting control, for example retaining more than 50 per cent of the votes. In the past, many foundation-owned (**p.69**) companies therefore issued dual-class stock, which allowed the foundations to retain absolute control by holding on to the (A) shares with high voting rights, while outside investors bought (B) shares with low voting rights. However, in recent decades, institutional investors have refused to take part in dual-class share issues, which results in no new issues of dual-class stock.

Compared to co-operatives, mutual organizations, or family trusts, industrial foundations are distinguished by irrevocability. The foundation cannot be dissolved except in bankruptcy or (theoretically) by the Foundation Authority, and the endowment cannot be paid back to founders.

4.3 Theoretical Considerations

According to what is known as 'the theory of the firm' in economics, there are a number of reasons why foundation-owned firms should fail, or at least underperform. They lack the profit incentive extolled in economics since Adam Smith. They are insulated from the market for corporate control, and are limited in their ability to diversify risk, as recommended in corporate finance.

Foundation boards lack the accountability emphasized in political science and management theory, since they refer essentially to no one but themselves.

Therefore, foundation ownership should theoretically be a recipe for disaster, and under specific circumstances, it might be. However, as we document in this chapter, under other circumstances, foundation-owned companies appear to function well and outperform conventional ownership structures. Therefore, it is worthwhile to consider what those circumstances might be.

Firstly, the profit motive may be less beneficial than is commonly assumed, since it involves an incentive to opportunistic behaviour, from which private shareholders may benefit. Sometimes, such opportunistic incentives may create market failures so great that both customers, companies, and the rest of society are better off with non-profit ownership, as emphasized in the theory of commercial non-profits (Hansmann, 1980). This could mean that foundation ownership would be more effective in businesses with information asymmetries such as R&D intensive firms, which in fact is consistent with the empirical evidence (Thomsen, 2017).²

Secondly, the profit motive may be less necessary than commonly assumed if executives and directors identify with the objectives of the organization (in this case the foundation), as emphasized in identity economics (Akerlof and Kranton, 2010). Foundation board members do not have profit incentives, as they manage the foundation's money and not their own, but for many reasons (**p.70**) they would generally prefer the foundation to own a successful business rather than an unsuccessful. For example, this could mean more money to donate to charity and greater prestige for the directors. Moreover, foundation directors have a fiduciary duty to the foundation, for which they are legally responsible.

Identification may be supported by proper organizational arrangements, for example what Hansmann and Thomsen (2013a) call 'managerial distance' between the foundation and the company it owns. The key idea is to measure the extent to which foundation and company are co-governed/managed as a single entity. The more independent the two entities (foundation and company), the higher the managerial distance. For example, high managerial distance would mean an independent foundation board which does not overlap with the board of the foundation-owned company. Distance between foundation and company may also increase with public listing, ownership dilution, and charitable foundation objectives, which imply that the interests of the two entities may diverge.

Social control, morality, and reputation effects may also play a role in keeping directors honest. It may be no accident that foundation ownership is particularly common in Northern Europe, which scores high on indices of governance, trust, and corruption control (Thomsen, 2016a, 2016b). Incidentally, the same countries have high tax rates, which reduces the effectiveness of monetary rewards.

Thirdly, industrial foundations are long-term owners, which may give foundation-owned companies a competitive edge in some business, for example in R&D intensive firms with long product life cycles (Børsting et al., 2016). We hypothesize that the advantages of long-termism are more pronounced in large firms than small start-ups for which product market competition is presumably more intense. On the same note, profit incentives matter less in large organizations, which by necessity have to delegate decision power to

professional managers. Large, well-consolidated firms may also be less capital constrained, and the inability to dilute ownership may therefore be less of a handicap for them.

Altogether, given the theoretical costs and benefits of foundation ownership, we do not have a clear prediction about the performance of foundation-owned companies.

4.4 Empirical Performance Studies

The performance effects of foundation ownership have mainly been studied by statistical regression analysis, in which a performance measure—for example profitability—is regressed on foundation ownership (dummy variable) controlling for other variables as firm size, industry, and time period which may influence performance independently of foundation ownership. Profitability may in turn be measured by ROA—return on assets (e.g. Ebit—earnings before **(p.71)** interests and taxes/assets), ROE—return on equity (net income/equity), or other measures.

Such methods make it notoriously difficult to establish causality. In itself, regression analysis can only establish correlation. To test for causality, researchers can apply a range of techniques, including instrumental variables, Granger-causality, and difference-in-differences, but they require exogenous variation in foundation ownership (i.e. variation not attributable to firm performance), which is difficult to establish since foundation ownership is in most cases stable over time.

Moreover, the choice of performance measure is subject to debate. For example, it is not clear that accounting profitability is the relevant yardstick, since foundation-owned companies arguably pursue a broader set of objectives. From a social point of view, productivity or employment growth might be more important measures. Moreover, ROA and other accounting-based performance variables suffer from well-known measurement problems, which may bias statistical estimation. Nevertheless, it is interesting to see if foundation-owned companies remain competitive even on the most conventional capitalist performance measure.

4.4.1 Denmark

While we can find foundation ownership on a global basis, their frequency is higher in Denmark than in other countries. The three largest Danish companies—Novo Nordisk, A. P. Møller Mærsk and Carlsberg—are all foundation-owned. Thomsen (2017) estimates that foundation-owned companies account for 5 per cent of Danish employment, 10 per cent of value added, 50 per cent of R&D, and 70 per cent of stock market capitalization.

There have been a number of academic studies of foundation ownership and firm performance.

Profitability: Thomsen (1996) compares foundation-owned companies to investor-owned and family-owned companies in a sample taken from the 300 largest non-financial Danish companies 1982–92. He finds no significant differences in accounting returns (ROE, ROA) or sales growth. However, foundation-owned companies appear to have significantly higher profit margins and significantly lower asset turnover. Moreover, foundation-owned companies are found to have significantly higher solvency (equity/assets) and lower earnings volatility (standard deviation of return on equity).

Thomsen (1999) explores possible explanations for the relatively good performance of foundation-owned companies. He is able to reject explanations based on market power (monopoly rents), tax advantages, or monitoring by minority investors and creditors. There is a tendency for better performance in foundations with a founding family presence, but the effect is not strong enough to explain the overall performance of foundation-owned companies. However, **(p.72)** he finds that the relative performance of foundation-owned firms deteriorates with company age.

Thomsen and Rose (2004) examine the stock-market performance of foundation-owned companies listed on Copenhagen Stock Exchange 1996–99. In a sample of 171 companies, twenty were majority-controlled by industrial foundations. They find that these foundation-owned companies are as efficient as other listed companies in terms of risk-adjusted stock returns, accounting returns, and firm value (Tobin's Q).

Hansmann and Thomsen (2013a) compare listed and unlisted Danish and Swedish foundation-controlled companies to listed Nordic companies 2003–9. They find that unlisted foundation-owned companies underperform listed companies matched by industry and size, while listed foundation-owned companies outperform in terms of accounting profitability (ROA) and firm value. Regardless of control group, the foundation-owned companies have less volatile earnings and slower growth than other listed companies.

Børsting et al. (2014) study the relative performance of all Danish foundation-owned companies from 2000–12, including a number of smaller, unlisted companies, which were not covered by previous research. They find that foundation-owned companies have lower overall accounting returns (ROA) and lower sales growth than other companies, but higher factor productivity and similar rates of productivity growth. However, the results are found to depend on firm size. Large foundation-owned firms outperform other large firms in terms of ROA, while small foundation-owned firms underperform other small firms. Since the large firms account for the bulk of the economic activity, foundation-owned companies outperform in terms of size-weighted averages. The authors also find that foundation-owned companies tend to have lower risk

(volatility of earnings) and they find no differences in risk-adjusted accounting returns.

Kuhn and Thomsen (2015a) study performance determinants (performance drivers) within foundation-owned companies from 2000–12, i.e. what factors make some foundation-owned companies perform better than others, and to what extent these factors are unique to foundation-ownership or apply to other companies. They find that the performance of foundation-owned firms is driven by firm size, equity share, research and development activity, board independence, and industry effects. Of these, the positive effect of firm size and R&D activity appears to be unique to foundation-owned firms, i.e. they do not drive performance in other companies.

Kuhn and Thomsen (2015b) study the effects of changes to foundation ownership using a difference-in-differences framework where firms changing to foundation ownership are compared to matching firms that do not. They find no significant effects on firm performance after change to foundation ownership, i.e. firm performance remains statistically undistinguishable from that of the control group.

Growth: Generally, empirical research has found that foundation-owned firms have lower, but more stable growth rates than other firms. For example, **(p.73)** Børsting et al. (2014) find that Danish foundation-owned companies grew by 4.8 per cent a year over the period 2000–12, while other firms grew by 6.7 per cent on average. Hansmann and Thomsen (2013b) find that foundation-owned firms have lower growth rates than a range of comparable control groups. One reason for lower sales growth may be that foundation-owned companies are less likely to dilute their ownership by M&A, since foundations desire to maintain their controlling influence. Foundations tend to prefer lower, more conservative financing and to resist borrowing to pay for acquisitions.

Productivity: Børsting et al. (2014) find that foundation-owned companies have higher levels of total factor productivity than other firms, but average rates of productivity growth. Kuhn (2015) finds evidence of higher labour productivity (value added per employee) in foundation-owned firms.

4.4.2 Sweden

There are two dominant spheres in Swedish business, which account for the majority of the nation's large companies—The Wallenberg sphere and the Handelsbank sphere. Both are based on foundation-ownership. A sphere is understood to be something less unified than a business group, but nevertheless connected by ownership and interlocking board members and managers. The subsidiary companies will typically not be majority-owned, but rather controlled by dominant minority positions.

Investor AB is a Swedish investment company founded by the Wallenberg family in 1916. The Wallenberg Foundations (mainly Knud and Alice Wallenberg's foundation) have a controlling influence in the company, with more than 50 per cent of the votes and 23 per cent of the capital. With no more than seventy-six employees at headquarters, Investor AB controls more than 600,000 employees in the subsidiary companies. The Wallenberg Foundations also own a private investment company, FAM, which has substantial holdings of its own (Thomsen, 2017).

Handelsbanken is at the centre of the other dominant sphere. Svenska Handelsbanken AB is a Swedish bank founded in 1871. It is effectively controlled by a number of foundations and associated companies (chief among them the Oktogonen Foundation (10.3 per cent) and Industrivärden (10.3 per cent). Compared to other banks, Handelsbanken has good financial performance and it came through the financial crisis relatively unscathed.³

Apart from the giant spheres (Wallenberg and Handels), there are a limited number of independent foundation-owned companies, among which we may mention Trelleborg and NCC.

Finally, IKEA is a one of the most interesting foundation-owned companies of Swedish origin.

(p.74) Dzansi (2011) compares the investment performance of 26 listed Swedish companies with foundation ownership of more than 20 per cent to that of other listed companies. Investment performance is measured by marginal firm value (marginal Q), defined by growth in market value relative to growth in the stock of invested capital. Dzansi finds that foundation ownership has a positive investment performance (marginal Q) relative to dispersed ownership, but the effect is not significantly different from the effects of other majority shareholders such as institutional investors and families. In other words, he finds that foundation-owned firms perform as well as other majority owners and better than companies with dispersed ownership.

4.4.3 Norway

Although Norwegian foundation law is quite open to industrial foundations, the structure is used by Norwegian businesses much less than it is in Sweden. However, we have been able to identify three specimens: Norske Veritas (an insurance company), Kavli (a food producer) and Thon (a property company). For a case study of Kavli, see Thomsen (2015).

In addition to these 'normal' industrial foundations, there are a number of ownerless Norwegian savings and loans associations (*sparbanker*) and insurance companies (such as Gjensidiga), many of which have recently been reorganized as foundation ownership. The savings and loans banks were historically not owned by shareholders, but governed by their stakeholders including depositors,

who elect a board of representatives electing the board of directors. Bøhren and Josefsen (2013) study the performance of the ownerless banks 1985–2002 compared to for-profit shareholder-owned banks and a hybrid non-profit form, which issues securities to the market. They find that the ownerless banks have the highest performance over the period as a whole, with ROA of 0.88 per cent compared to 0.32 per cent in for-profit commercial banks and 0.42 per cent in the hybrid banks. The differences were significant during the Norwegian banking crisis (1988–92), when the ownerless banks outperformed commercial banks, as they were financially more conservative. These differences are robust to various kinds of statistical control including bank size effects.

4.4.4 Germany⁴

Many industrial foundations exist in Germany, with large foundation-owned firms such as Bertelsmann, Bosch, Körber, Mahle, ThyssenKrupp, and ZF Friedrichshafen.

(p.75) Most of these appear to have been established by the entrepreneurs who founded the companies, or their descendants, in order to ensure the continuation of the company. However, regulatory arbitrage may be another motive (Draheim and Franke, 2014). Some family foundations are fully liable general partners in foundation-owned partnership firms (*Kommanditgesellschaft*). They have no equity stake and no claim on the firm's profits, but are fully liable for the firm's liabilities and possess the voting rights. As general partners, the foundations get a fixed fee for management and risk-bearing, but their assets tend to be small. The reason for setting up this type of family foundation is presumably to ensure that founding family members have limited liability. Moreover, disclosure (such as publishing annual reports) was historically more limited for partnerships.

According to Draheim and Franke (2014), another motive may be to bypass the German codetermination law. Companies with many employees are subject to mandatory codetermination (employees elect one-third of the board members in companies of more than 500 employees, and half in companies with more than 2,000 employees). Companies like Aldi and Lidl, two large retail store chains, have set up various small regional partnerships which own the supermarkets and are not subject to codetermination. The family foundations are similar to holding companies of the regional partnerships.⁵

Regulation of foundations is mostly governed by the individual German states, rather than at the federal level, since the foundation charter has to be approved by the state in which the foundation is registered. It is difficult to change the charter once it has been approved by the state.⁶ The foundation charter specifies the purpose of the foundation, restricts its activities, and prescribes how it should be managed. The foundation charter should assure the long-term survival of the foundation, and foundations are obliged to preserve their capital base. For

example, they are not allowed to pay out to beneficiaries if this would undermine their capital base. Moreover, the foundation is usually not allowed to sell its shares in the company.

There appear to be important differences between German states in regulating foundations (Draheim and Franke, 2014). Baden-Württemberg is regarded as being highly restrictive in granting tax-exemption only if the foundations do not participate in the management of their owned firms. Presumably, this is why the Bosch and Mahle foundations are set up as corporations, in order to avoid any influence of the state office. Since both foundations own almost all of the equity claims but have no voting rights, a separate management company is set up with a strong position in the supervisory board of company.

(p.76) The strict tax-related policy of Baden-Württemberg does not apply in other German states like North Rhine-Westphalia or Hamburg, where a charitable foundation may interfere in the management of its company without endangering its tax privileges—for example foundation managers may have a strong influence on the board of the company.

Herrmann and Franke (2002) find no significant performance disadvantage to foundation-ownership in Germany. On the contrary, profitability tends to be somewhat higher, but differences disappear when controlling for other relevant variables. In subsequent work based on matched samples, Draheim and Franke (2015) find that German foundation-owned companies tend to have lower ROA, although the difference is typically not statistically significant.

Draheim and Franke (2014) examine the performance of the German foundation-owned firms relative to control firms matched by size and industry. They find that return on assets in foundation-owned companies tends to be smaller relative to matching firms. The difference in ROA is not significant, but the foundation-owned companies have significantly lower return on equity (ROE). This may partly be a result of foundation-owned companies having more employees (because they pay more attention to stakeholders) and partly because they pursue a more conservative financing policy with lower leverage and less risk.

Achleitner et al. (2017) study share price reactions to fifty-two announcements of increases or decreases in foundation ownership of listed German firms. Using financial event study methodology they find positive reactions to twenty-two announcements of decreases in foundation, but no significantly negative reaction to thirty announcements of increases.

4.4.5 Austria

There are two distinct kinds of foundations in Austria—private foundations and public benefit foundations, each based on distinct bodies of law.⁷ In contrast to public benefit foundations, private foundations are not required to serve a public

benefit purpose, but may, for example, support a founding family, a company, or other private goals.

At first glance, there are a large number of industrial foundations in Austria, but on closer inspection, many of them turn out to have government links, which takes them somewhat apart from our conception of foundations as private entities. However, we have identified two companies which fit the bill: A-TEC Industries and Styria Media Group. Like Italy and Norway, Austria has a large number of banking foundations which own former savings and loans associations (*Sparkassen*).

(p.77) 4.4.6 Switzerland

Industrial foundations are termed corporate foundations in Switzerland and more precisely holding foundations.⁸ They have been the subject of some debate as they pursue an economic function, but were officially recognized by The Swiss Federal Court only in 2001. In spite of the lack of transparency surrounding Swiss foundations and private companies,⁹ we have been able to identify two interesting foundation-owned companies—Rolex and Victorinox.

4.4.7 The USA

Legally, US foundations can be set up as trusts or non-profit corporations. Trusts differ from European or Danish foundations, which are legal persons and subject to a specific body of foundation law. Moreover, both trusts and non-profit corporations are flexible organizational forms, which can be used to structure almost any kind of economic organization, including investment companies, banks, and charities. However, the term foundation is widely used in the US, and it is possible to structure a trust in such a way that it is functionally identical or at least similar to a foundation, the defining features of which are irrevocable separation from the founder, independent governance, and a well-defined (non-selfish) purpose.¹⁰

Currently, industrial foundations are rare in the United States, but apparently they were not uncommon before the 1969 foundation laws, which effectively prevent US foundations from having ownership control of business companies (Fleishman, 2001). For example, the Ford Foundation was apparently originally conceived as an industrial foundation that was to control a majority of the stock in Ford Motor Company.¹¹

The 1969 Foundation Law (House of Representatives, 1969) 'limits to 20 per cent the combined ownership of a corporation's voting stock which may be held in the future by a foundation and all disqualified persons together'. The argument was that

Those who wished to use a foundation's stock holdings to acquire or retain business control in some cases were relatively unconcerned about producing income to be used by the foundation for charitable purposes. In

fact, they might have become so interested in making a success of the business, or in meeting **(p.78)** competition, that most of their attention and interest was devoted to this with the result that what was supposed to be their function, that of carrying on charitable, educational, etc., activities was neglected. Even when such a foundation attains a degree of independence from its major donor, there is a temptation for its managers to divert their interest to the maintenance and improvement of the business and away from their charitable duties. Where the charitable ownership predominates, the business may be run in a way which unfairly competes with other businesses whose owners must pay taxes on the income that they derive from the businesses. To deal with these problems Congress concluded it is desirable to limit the extent to which a business may be controlled by a private foundation.

The law is sanctioned by a tax on excess business holdings,¹² defined as holdings above 20 per cent of the stock in a single company (including the holdings of disqualified related persons).¹³ The penalty is, in the first instance, a tax imposed on the foundation equal to 10 per cent of the value of such holdings. However, if the foundation still has excess business holdings at the close of the taxable period, a tax equal to 200 per cent of such excess business holdings is imposed. Understandably, few foundations want to have any such holdings.

The 1969 Law refers to an increasing use of the foundation structure as a shelter for business activity and mentions a number of examples of abuse. For example:

The A foundation holds controlling interests in 26 separate corporations, 18 of which operate going businesses. One of the businesses is a large and aggressively competitive metropolitan newspaper ... Another of the corporations operates the largest radio broadcasting station in the State. A third, sold to a national concern as of the beginning of 1965, carried on a life insurance business. Among the other businesses controlled by the foundation are a lumber company, several banks, three large hotels, a garage, and a variety of office buildings. Concentrated largely in one city, these properties present an economic empire of substantial power and influence.

Fleishman (2001) summarizes and criticizes the arguments put forward for the US excess business holding provisions in the 1969 law:¹⁴

- The unfair competition argument, according to which foundation ownership would subsidize foundation-owned companies by lower required rates of return, thus giving them an unfair advantage against investor-owned companies. However, Fleischman argues that

subsidies of this kind are already effectively prevented by other parts of foundation law.

- The diversion of attention argument, according to which the foundation would be unable to simultaneously perform the two roles as corporate **(p.79)** owner and donor in an effective way. Fleischman does not find this argument persuasive for large foundations, which can afford to set up separate offices for the two functions.
- The personal material benefit argument, according to which founders may receive benefits from tax-sheltered wealth and income in the foundations. Fleischman observes that this kind of abuse is not unique to foundations and that it is in any case addressed as an offence in other parts of foundation law.
- The inadequate dividend income argument, that foundation ownership would lead to a preference for retained earnings in the company. Since foundations may require continuous financing of their expenses, it is not clear that foundations will be less inclined to require dividends from the company.

Fleischman concludes (2001: 394) that ‘We arrive at what seems to be an inescapable conclusion therefore, that the US excess business holding provision in its present form was, simply put, a wrong-headed idea, unevenly applied. In other words, it probably shouldn’t have been enacted at all.’

One might wonder why, in a country with a strong tradition for liberalism and freedom of contract, the rule was enacted anyway. Using a term from the legitimacy literature, one reason may be a lack of ‘isomorphism’ (or fit) with elements of the market-based governance system, in particular the distrust of concentrated power and the inclination to reproduce ‘democratic’ governance structures in corporate governance (Thomsen, 1996).

In any case, the 1969 laws have virtually eliminated industrial foundations in the US, and we have only been able to identify one foundation-owned US company which comes close to foundation ownership—Hershey. Another example of a parallel non-profit organization would be the Mayo Clinic, which runs a chain of hospitals.

4.4.8 The UK

Legally speaking, British foundations are trusts, rather than foundations in the European sense of the word. Charitable British trusts are supervised by the Charity Commission (the Charity Commission for England and Wales), which answers directly to the UK Parliament rather than to government ministers (Fries, 2010). The Charity Commission appears to be no less sceptical than the US authorities towards combining philanthropy with business.

We have been able to identify two industrial foundations that are currently active in the UK—Lloyd's Register and the Guardian Media Group. In both cases, there is a strong sense of social mission (charity) in the activity conducted by the companies. This may be one reason why they have been allowed to continue.

(p.80) The Wellcome Trust was previously a good example of a well-performing British Industrial Foundation. The Trust produced vaccines for tropical diseases and discovered Retrovir (AZT), the first chemical compound active against HIV/AIDS. Wellcome subsequently merged with Glaxo to become Glaxo-Wellcome (currently renamed again to Glaxo). The Wellcome Trust is now a purely charitable foundation which funds a large part of private-sector research in the UK. Interestingly, the merger with Glaxo was partly motivated as being in the best interest of the company.

4.4.9 France

The foundation sector in France is generally regarded as less developed than in other European countries, partly because the French state has been suspicious of foundations and regulated them heavily until the first foundation laws in 1987 (Archambault, 2001; Deckert, 2010). The government appears to have viewed foundation involvement in business activity with even greater suspicion, partly because of the tax benefits which foundations obtain. However, in recent years this regulatory climate appears to have changed. Pierre Fabre—the third largest French pharmaceutical company—is foundation-owned.

4.4.10 The Netherlands

Industrial foundations are common in the Netherlands, but are best known when used as a takeover defence. A company can set up a foundation, often as a so-called administrative office (*Administratiekantoor*), which owns or controls the voting rights of preferred shares while the cash flow rights are issued to the public (De Jong et al., 2007; Rosenboom and van der Goot, 2003). The foundation, which is effectively controlled by (or at least influenced by) company management, exercises majority control (or at least controlling influence) of the company. Alternatively, a foundation may own an option to call preferred shares in case of a takeover and place them with friendly investors. These mechanisms effectively short-circuit the corporate governance system, eliminating checks and balances on company management.

This managerialist structure played a role in an accounting scandal at Royal Dutch Ahold, a large Dutch retailer, in which a foundation—Stichting Administratiekantoor Preferente Financieringsaandelen Ahold—controlled 63 per cent of the votes (De Jong et al., 2007).

4.4.11 Italy

Foundations play an important role in Italy as bank owners (The Economist, 2001; Frye, 2013). The Italian banking foundations were created by the privatization **(p.81)** of public and semi-public financial institutions after the so-

called Amato Law was passed in 1990 (Leardini, Rossi, and Moggi, 2014). Under the law, more than eighty savings banks and a number of credit institutions, including Monte dei Paschi di Siena (which claims to be the world's oldest bank), were required to spin off their banking activities into joint-stock corporations. Ownership of the shares went to newly established charitable foundations.

The banks became publicly listed commercial enterprises, while the foundations continue to hold sizeable and in many cases controlling share positions. Around two-thirds of Italian bank assets are directly or indirectly owned and controlled in this way. Important examples include Unicredit and Banca Intesa—as well as Banca Monte dei Paschi di Siena, which has recently been beset by financial difficulties. In total, there are around eighty-six banking foundations. The foundations are grant-making charitable organizations with other financial investments in addition to the bank shares. Nine of the ten largest Italian foundations are banking foundations (Nadège, 2014). Grants go mainly to the local region of the bank.

The banking foundations appear to have supported consolidation and modernization of the Italian banking sector as well as international expansion, while serving as responsible long-term shareholders and sources of recapitalization during the financial crisis (Nadège, 2014). However, their finances have deteriorated and their portfolios are concentrated on their bank stocks. Moreover, they have been criticized for political influence, since most foundation board members are directly or indirectly elected by local authorities, and local politicians dominate their boards. The foundations are also criticized for lack of transparency and effective supervision. Foundation-owned banks are found to have a larger proportion of non-performing loans, to have less core capital, and to be more vulnerable to macroeconomic shocks (Nadège, 2014). The Italian central bank has recently pushed the foundations to loosen their ties to the banking sector.

The Italian case demonstrates that the effectiveness and performance of industrial foundations depend on corporate governance. If foundation boards are filled with politicians, the chances are that they will not be effectively governed.

4.4.12 India

One of the most admired companies in India, and in the world in general, turns out to be foundation-owned. The Tata Group¹⁵ is a large Indian conglomerate. It has twenty-nine listed subsidiaries and more than eighty operating businesses (2012). It has shown strong financial performance and **(p.82)** social responsibility for decades. The main holding company, Tata Sons, is majority-owned by charitable trusts.

In addition to excellent financial performance, the Tata Group is outstanding for social responsibility. Both group companies and the owner trusts engage deeply

in philanthropic activities. Moreover, the Trusts and the Group are governed by a code of conduct, which is taken serious and rigorously enforced. The code specifies for example that Tata companies must benefit the countries and communities in which they operate, support competitive open markets, provide equal opportunities to all employees, strictly avoid corruption and maintain political independence, and be committed to shareholder value.

4.4.13 Taiwan

Foundations are widely used as part of family business groups in Taiwan. Nearly every family business group has an associated foundation which holds shares in the company. However, the typical shareholdings are small minority shares of 5 per cent or less. One hypothesis is that such holdings play a role in manifesting extended family or clan ownership of Taiwanese companies, since foundations can be staffed by family members and help maintain family control.

However, there are examples of more dominant foundation control in Taiwan. The founder of Taiwan's largest company, Formosa Plastics Group, Mr Wang Yung-Ching donated his shares to the Wang Chang-Gung Foundation, which has philanthropic goals but also serves as the controlling shareholder of the four publicly listed affiliated firms in this group (Fan, Li, and Leung, 2010). In total, the group has more than 106,000 employees.

4.5 Conclusion

Foundation-owned companies or their functional equivalents are found throughout the world, although they are nowhere as common and as important to the national economy as in Denmark. Some of the world's largest and most admired companies are owned in this way, which testifies to the competitiveness of the foundation model.

The academic literature on the performance of foundation-owned firms is not large, but the empirical studies as well as anecdotal evidence appear to indicate that foundation-owned companies roughly perform on a par with other companies.

In many countries, including the US and UK, existing laws would need to be changed to allow industrial foundations. In particular, governments would need to recognize that business ownership can be a legitimate objective for **(p.83)** foundations (trusts). To prevent abuse, a body of law similar to the Danish law on industrial foundations and the law on taxation of industrial foundations would be necessary. Foundation law should ensure that donations to foundations are irrevocable and that foundations cannot in return donate to the founders or their family. Foundations should have independent boards and be monitored by a government agency like the UK Charity Commission, to which they should submit audited annual reports.

This involves some administration costs, but the upside is that visionary founders can find a secure ownership base for their companies.

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Notes:

(¹) In this section we try to summarize some essential institutional characteristics of industrial foundations based on Thomsen (2017: chapter 3, 8, and 9). Most of the material relates to research on Danish data. It is not clear to what extent the description is valid outside Denmark.

(²) In addition, Hansmann (1996) mentions information asymmetry as a possible explanation for mutual and non-profit ownership of financial institutions. There are in fact a number of foundation-owned and mutual financial institutions in Denmark and elsewhere.

(³) <http://www.gurufocus.com/term/ROA/SVNLY/Return%20on%20Assets/Svenska%20Handelsbanken>.

(⁴) This section builds on Draheim and Franke (2014).

(⁵) Another motive appears to be to stabilize the ownership structure of the chain stores by transferring ownership to the family foundations.

(⁶) The state offices responsible for foundations also supervise the annual statements of foundations.

(⁷) See http://www.slogold.net/foundations_in_austria.html.

(⁸) See http://www.rwi.uzh.ch/lehreforschung/alphabetisch/jakob/lehre/unterlagenfs12/artmarketstudies12/EMAMS_Foundation_Law_Reader.pdf, p. 3.

(⁹) See <http://www.icnl.org/research/journal/vol16iss1/swiss-legal-framework.pdf>.

(¹⁰) See Chapter 3 section 3.2.3.3.

(¹¹) In Ford, the foundation held cash flow rights (non-voting shares), while the Ford family held the voting rights (Ellis, 2008), which created substantial technical problems when the company was taken public (Ellis, 2008).

(¹²) See Code 26 US Code § 4943.

(¹³) The limit may be raised to 35% if it can be demonstrated that a third party has majority control of the company.

(¹⁴) This section builds on Thomsen (2006).

(¹⁵) This section draws on Thomsen (2012).

