1. Introduction

The aim of this book is threefold. The first aim is to provide a review of the legal aspects of corporate governance with particular emphasis on the objective of the corporation. The literature review starts with a discussion of the division of powers in the corporation and the role of owners and management in corporate governance. It then proceeds by analysing the role of stakeholders as well as that of gatekeepers as actors in corporate governance. The second aim is to investigate whether corporate governance affects performance. Some of the current major challenges that researchers are facing are uncovered. One of these major challenges includes the potential endogeneity of corporate governance characteristics. Ownership is one of the corporate governance characteristics that may be endogenous. While early studies on the link between ownership and firm value have assumed that ownership is a given, i.e. is randomly determined, more recent studies have revealed evidence suggesting that the current ownership structure of a corporation depends – at least to some extent – on its past financial performance. Hence, financial performance may not only be the result of the firm’s ownership (as well as other corporate governance characteristics), but it may also shape the latter. The third aim is to introduce complexity theory and to explain how its concepts may be used to fill in the gaps in the existing corporate governance literature. In particular, complexity theory may provide a way forward to deal with the frequently complex relationships between the corporation on the one hand, and its stakeholders and gatekeepers on the other hand. To date, the extant literature that uses concepts from complexity theory is very limited. Further, the sparse literature that exists tends to focus on one or a few complexity principles while ignoring others, similarly important concepts. While the authors of this book do not claim to provide a solution to all the unsolved key problems in corporate governance research, they nevertheless hope that this book will provide a way forward to address some of the more complex issues with the help of complexity theory as a lens.

This book is organized as follows. Chapter 2 introduces complexity theory and discusses how complexity theory may be used for the study of corporate governance. In addition, this chapter also reviews how insights from complexity theory may be used by individual organizations as well as entire industries and economies to create enabling environments that facilitate good corporate governance.
governance. These insights are illustrated via (and to some extent derived from) the study of a case company, a large UK multinational. While corporate governance is an area which has gained an increasingly high profile in the last decade with interest from the academic and non-academic communities alike, despite the widespread adoption of corporate governance codes, financial scandals and collapses still occur. It seems that a rethinking of corporate governance frameworks is therefore overdue and this chapter provides both theoretical and practical insights that may contribute to such rethinking. Complexity theory explains the behaviour of complex adaptive systems. When we think of a governance framework, we think in terms of internal and external actors or participants interacting with each other. Internal actors in a company include the directors and employees, external actors include the shareholders and wider stakeholder groups, plus the legal, social and political influences and structures. Complexity theory emphasizes the relationships, connectivity and interdependence between the internal and external actors, and the various structural influences on the environment in which they operate. By identifying, and analysing, the multiple elements that interact and influence each other, we will gain a deeper understanding of the evolution of governance frameworks, and reveal new insights regarding their effectiveness.

After the introduction to complexity theory and complexity theory’s potential input into the study of corporate governance, the book proceeds by discussing corporate governance issues in more detail, including the identification of gaps in the extant academic literature (Chapter 3 and Chapter 4). The penultimate chapter of the book, Chapter 5, then reviews the as yet limited literature using complexity theory to study corporate governance. Chapter 6 concludes with some policy implications and suggestions for further research.

Chapter 3 focuses on the legal aspects of corporate governance while Chapter 4 focuses on the financial aspects. Chapter 3 starts by studying the division of powers in the corporation, with particular emphasis on the roles of shareholders and managers in corporate governance. Although an international perspective is adopted, there is a clear focus on the UK in this chapter of the book. Indeed, the recent Company Law Review in the UK (which culminated in the Companies Act 2006) suggests a shift from the principle of shareholder supremacy to the enlightened shareholder approach. Conversely, company law in most other countries of the world has traditionally been driven by a stakeholder- rather than a shareholder-centric view. Hence, it can be argued that, although the recent Company Law Review in the UK represents an as-yet small change, this change may have paved the way for a possibly much larger future paradigmatic shift in UK law towards a more stakeholder-oriented model of corporate governance. After discussing the division of powers in the corporation, Chapter 3 then proceeds by reviewing the role of stakeholders, such as employees and customers, as well as the role of gatekeepers. Recent
regulatory developments, such as the Sarbanes-Oxley Act (2002) in the USA, have put more emphasis on the role of gatekeepers in monitoring management of corporations and limiting or even avoiding corporate fraud. The pros and cons of enrolling gatekeepers are reviewed, followed by a discussion of the complex nature of the relationships between the corporation and its gatekeepers.

Chapter 4 of the book is on the link between corporate governance and firm performance. While the question as to the impact of corporate governance on firm value and performance is a crucial one, its analysis is not straightforward for at least two reasons. The first difficulty that the researcher encounters relates to the definition and measurement of performance. While the measurement of firm performance may be relatively straightforward if an investor perspective is adopted, it is much less so if the perspective is that of other types of stakeholders. In addition, existing research suggests that the link between financial performance and corporate governance is not necessarily linear and unidirectional. Indeed, recent research suggests that corporate governance characteristics may also be affected by past performance and not just vice-versa. Finally, research also suggests that corporate governance devices do not act in isolation. For example, the presence of one corporate governance device may limit the usefulness of another one and vice-versa.

Chapter 6 concludes the book by proposing a way to reassess the key issues raised in Chapters 3–5. The proposed way forward is complexity theory. Complexity theory suggests a series of concepts and principles which are likely to help scholars of corporate governance and practitioners alike with the analysis of the key issues. In particular, complexity theory is a way forward to visualize, describe and investigate the often-complex relationships between a corporation on one side and its owners, stakeholders and gatekeepers on the other side.