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Discussion of

Workers in the Board Room: The Causal Effects of Shared Corporate Governance

(Jäger, Shoefer, Heining)

by Jonathan Cohn

Research question

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- Since WWII, German law has given labor representation on company supervisory boards
- How does labor representation on boards affect company behavior/outcomes?
  - Dark side (for companies): Rent extraction, distortions
  - Bright side: Labor buy-in, information-sharing (but wouldn't companies voluntarily adopt?)
  - Irrelevant?
- More general question: Does board structure really matter?

This paper

- Ideal experiment: Take two identical companies, give labor representation on board of one but not the other
- Empirical challenges: Variation in board labor representation limited, not orthogonal to important firm characteristics
- This paper: Studies 1994 reform removing mandatory labor representation for new companies w/ fewer than 500 employees
- Two empirical approaches:
  - RD: Compare outcome variables at firms incorporated just before and just after reform
  - Diff-in-diff: Compare differences in outcomes variables at firms incorporated before and after reform (1st diff) to differences for non-corporations (2nd diff)

Main findings

- Shared governance → more women, fewer PhDs, fewer aristocrats on supervisory board
- Shared governance → more fixed assets, higher low-skilled employee %, lower cost of debt
- No statistically significant effect on profitability, employment, wage bill (total or per employee), revenue (total or per employee), value-added (total or per employee), outsourcing, total assets, current assets, high-skilled employee %, medium-skilled employee %, leverage, debt maturity structure, most financing constraint & distress variables (e.g., KZ, HP, WW, Z score)

Summary of thoughts

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- Impressive data collection exercise, tight experiment
- Couple of comments on empirical strategy
- River of results (actually, mostly non-results)
- No obvious coherent <u>affirmative</u> takeaway
- One possible takeaway: Shared governance is not important
- This would be an important conclusion
- Might be more to learn from time series

Treatment of controls?

- Ideally, treated get treatment, controls get no treatment
- Competitive spillovers -> controls get some treatment as well
- E.G., shared governance makes firm less competitive
  - Eliminating shared governance (treatment) makes a firm more profitable
  - Makes untreated competitors less profitable
  - Pure treatment effect directionally consistent but overstated
- Makes it difficult to estimate effects of treating all firms by implementing/eliminating shared governance universally
- Could look for evidence of spillovers

Survivorship

- Study isolated to firms started between August 1992 and August 1996 (two years either side of shock)
- Sample period = 1994-2016
- Would imagine that a lot of firms disappear between 1994 and 2016
- Possible sources of bias?
  - Bankruptcy: Non-shared governance firms less resilient, weaker ones disappear
  - Acquisitions: Non-shared governance firms have advantage, stronger ones less likely to be acquired
- Possible to look at these sources of disappearance?

Board composition

- Shared governance → more women, fewer PhDs, fewer aristocratic family members on supervisory board
- These differences seem likely to be mechanical
  - Non-shared governance: Directors appointed by shareholders, likely to be businesspeople
  - Shared governance: Portion of directors appointed by employees, most of these likely to be workers
  - Compared to businesspeople, workers more likely to be female, less likely to be PhDs, aristrocrats
- Do these differences matter?
- Differences in non-employee directors?

Shared governance irrelevant?

- Some lawsuits filed by firms incorporated before August 1994 seeking to shed employee representation requirement, but…
- No apparent change in incorporation frequency
- No apparent bunching below 500 employees post-shock (minimum threshold for shared governance)
- Paper looks at a large # of possible outcomes, few appear to be affected by shared governance
  - Seems plausible that the ones that vary do so by chance
  - Aside: Would imagine that errors in a lot of variables cluster over time at industry or regional level, might consider clustering at these levels (at least in diff-in-diff)

One other test of (ir)relevance

- Consider event study analysis (i.e., look at stock returns) around adoption of rule (may or may not be implementable)
- Shock only affects new firms, so no way to look at returns for these
- If shared governance makes firms less competitive, rule would have been bad for large, publicly-traded firms
- Especially for those in industries with a lot of entry/low barriers to entry

Financial crisis

- One possibility: Shared governance valuable in times of distress
- Workers may be more willing to renegotiate labor contracts in times of distress if they are represented on board
- Do firms w/ shared governance reduce wages but maintain employment, relative to other firms, in the event of distress?
- Sample period includes financial crisis period
- Are firms w/ shared governance more resilient during financial crisis (maintain higher employment, reduce wages, less likely to disappear)?