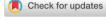**RESEARCH ARTICLE**

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Excess executive compensation and corporate governance in the United Kingdom and Spain: A comparative analysis

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Literature on executive compensation has relatively neglected the impact of institutional governance contexts. Regarding filling this gap, this study examines the influence of governance mechanisms on excess executive compensation comparing a set of listed UK and Spanish firms on an 8-year panel data. Findings indicate that Spanish firms are characterized by higher excess executive compensation than UK firms because of the less effectiveness of ownership structure and board of directors. Differences in concentration and structure of ownership as well as in composition and size of boards result in more aligned executive compensation design in the UK firms.

1 | INTRODUCTION

The compensation of executives has remained a hotly debated topic over recent years. Interest has increased further as a result of the financial crisis. In particular, the crisis has called into question the diligence of directors in the management of their firms. This is because, while firms in most countries experienced a marked reduction in profits following the crisis, their executive directors were seen to continue receiving excessively high levels of compensation, often higher than those that had prevailed in earlier times of economic expansion.

Central to agency theory (Jensen & Meckling, 1976) is the idea that a critical instrument for limiting the discretion of executives and focusing them on the maximization of firm performance is the design of executive compensation (Jensen & Murphy, 1990; Murphy, 2013). While some studies have examined the extent to which executive compensation is directly linked to firm performance, others have attempted to analyze whether those responsible for setting compensation packages—through various corporate governance mechanisms—have managed to establish a rational design of

executive pay that effectively aligns the interests of executives with those of the firm. Or whether, on the contrary, they have succumbed to the influence of executives, resulting in pay arrangements that reflect the particular interests of those executives (Bebchuk et al., 2002; Devers et al., 2007; Gomez-Mejia & Wiseman, 1997; Tosi et al., 2000).

The most influential governance mechanisms in determining executive compensation are generally seen to be the ownership structure and the composition of the board of directors. Past literature has studied the influence of these mechanisms, finding high correlations between various board and ownership structural characteristics and the degree of executive compensation alignment (Brick et al., 2006; Conyon, 2014; Core et al., 1999; Ozkan, 2011). However, the study of the institutional context in which firms operate has been relatively neglected, and yet it determines the effectiveness of all corporate governance mechanisms (Aguilera & Desender, 2012; Renders & Gaeremynck, 2012). As La Porta and colleagues show across various studies (Johnson et al., 2000; La Porta et al., 1998), governance mechanisms are neither universal nor equally effective in all countries. The institutional context of each territory influences the effectiveness of

governance mechanisms that, in turn, determine the degree of alignment of executive compensation (Baixauli-Soler & Sánchez-Marín, 2011; Cyert et al., 2002).

Although there are some extant studies that examine corporate governance across several countries (Conyon et al., 2011; Cucari, 2019; Paniagua et al., 2018; Renders & Gaeremynck, 2012), it is helpful to focus international comparisons in a deeper way that helps identify the specific effects of the various mechanisms of governance in different institutional settings. The United Kingdom and Spain are two European countries that differ in many aspects of corporate governance that could be expected to affect executive compensation. The dominant model of corporate governance in the United Kingdom is rooted in Anglo-Saxon common law, characterized by a high dispersion of ownership, a legal system very protective of minority shareholders, a high degree of information transparency, and a highly developed and liquid capital market that itself acts as an external control mechanism (Kirkbride & Letza, 2009; Weir et al., 2002). Spain, by contrast, has a model of corporate governance typical of Continental European countries. This is based on a civil law system, with a high concentration of ownership, the existence of multiple cross-holdings, a legal system less protective of minority shareholders, less transparency in disclosure, and a low level of development of capital markets (Baixauli-Soler & Sánchez-Marín, 2015; De Miguel et al., 2004; Leech & Manjon, 2002). These features lead to different types of agency conflict in each country. In the United Kingdom, governance mechanisms seek to align the interests between executives and shareholders—the principal–agent conflict. In Spain, however, the need to align interests between majority and minority shareholders—the principal–principal conflict (Johnson et al., 2000; La Porta et al., 1999; Young et al., 2008)—is paramount.

These dissimilar governance contexts may lead to differences between these countries in the effectiveness of monitoring, and therefore divergences in the control exercised over executives through compensation (Baixauli-Soler & Sánchez-Marín, 2011; Conyon & He, 2011). Thus, in line with recent calls for more comparative analysis of corporate governance (Cucari, 2019; Paniagua et al., 2018), the main goal of this study is to compare the influence of the ownership structure and the characteristics of the board of directors in the determination and efficiency of executive compensation between the United Kingdom and Spain. In so doing, we aim to examine the extent to which these various characteristics contribute to a more effective alignment of executive compensation with firm performance.

Utilizing a sample of UK and Spanish listed firms during the period 2005–2012 in a panel data methodology, this paper contributes to the corporate governance and executive compensation literature in several ways. First, to our knowledge, this is the first empirical study to compare in depth the corporate governance between the United Kingdom and Spain and their respective effects in executive compensation. Both countries exhibit key differences regarding both the role of the governance contexts and the firms' mechanisms of monitoring that influence the design of executive compensation (Brick

et al., 2006; Ozkan, 2011). The United Kingdom, representing an Anglo-Saxon system of governance dominated by principal–agent conflicts in the shareholders–executives in firms' relationships; and Spain, typical context of Continental European system of governance, dominated by principal–principal conflicts in the shareholders–executives in firms' relationships. Both governance contexts contribute to a better understanding of how mechanisms of monitoring influence on—and are effective to—executive compensation alignment. Second, we make use of differences in executive compensation efficiency through the fresh concept of "excess compensation," as an indicator of the deviation of optimal executive compensation, to help clarify how the degree of efficiency of the governance mechanisms that, under different contexts, impacts on the pay-for-performance alignment originating, in suboptimal cases, the excessive payment of executives (Brunarski et al., 2015; Chung et al., 2015). Third, this study not only includes agency considerations in explaining the links between governance and executive compensation, but also includes institutional arguments in order to produce a fuller picture of these relationships (Aguilera et al., 2008; Judge et al., 2008; Renders & Gaeremynck, 2012), enriching thus the explanation of executive compensation and the internal and external (institutional) factors that help to explain it. And fourth, empirically this study uses a remarkable empirical approach, based on the classic model of Core et al. (1999), which establishes the basis to explain on the ground of key variables the degree of optimal payment to executives. This approach (Alissa, 2015; Core et al., 2008; Sánchez-Marín et al., 2017) helps to identify more accurately the degree of efficiency of executive compensation in terms of alignment with firm performance and reduction of agency conflicts.

The structure of the research is as follows. First, we approach the main characteristics that differentiate the contexts of corporate governance in which the respective UK and Spanish firms operate. Second, we hypothesize about how these different characteristics influence the main mechanisms of governance of the UK and Spain companies—namely, the ownership structure and the board of directors—finally impacting on executive compensation. Third, we describe the data, the models, and the panel methodology employed. Fourth, we describe the results obtained. Finally, we discuss the main conclusions reached as well as the academic and practical implications.

2 | THEORETICAL FRAMEWORK AND HYPOTHESES

2.1 | Contextualization of corporate governance in the United Kingdom and Spain

Corporate governance has its main roots in agency theory (Jensen & Meckling, 1976). From the classical principal–agent perspective, the separation of ownership and control may allow the firm's executives to abuse their managerial discretion to make decisions that benefit their own personal interests, as opposed to maximizing firm value

(Berle & Means, 1932). Effective corporate governance involves installing a series of mechanisms that guide the actions of executives towards achieving the objectives desired by the owners of the firm by allocating the wealth invested by the firm in an appropriate way (Aguilera & Desender, 2012). To achieve this end, the owners have at their disposal a number of direct and indirect instruments of executive monitoring, mainly by means of the ownership structure of the firm and the composition, structure and functioning of the board of directors (Brick et al., 2006; Core et al., 1999).

However, beyond such concrete approaches to monitoring, the effectiveness of corporate governance is also conditioned by the institutional framework in which the firm operates (Aguilera et al., 2008). Because there is no universal model of corporate governance applicable to all national contexts (La Porta et al., 1999; Renders & Gaeremynck, 2012), it is necessary to identify the characteristics of the institutional context of a country in order to understand the specific corporate governance peculiarities that determine the effectiveness of the various monitoring mechanisms. In each country, firms try to adapt to their specific institutional environment—with its political, market, and legal considerations—resulting in diverse systems of corporate governance (Aguilera & Desender, 2012; Judge et al., 2008; Mezias, 1990).

There are two basic types of corporate governance models: the Anglo-Saxon system and the Continental European system. The institutional context in which UK listed firms operate is very different from that of their Spanish counterparts: while the United Kingdom is representative of an Anglo-Saxon model, Spain is typical of the model found in most Continental European countries (Faccio & Lang, 2002; La Porta et al., 1998). As a consequence, the type of control is usually very different in the two countries. In the United Kingdom, numerous shareholders own small proportions of the shares in a firm, take a more passive role in the defense of their interests, and consequently, usually delegate their proxy vote to the board of directors (Grossman & Hart, 1980; Maug, 1998). In this sense, the board's supervisory function may decrease if those executives also sitting on the board—executive directors—use their power to make decisions that benefit themselves, extracting rents at the expense of shareholders (Bebchuk et al., 2002; Hart, 1995; O'Reilly et al., 1988, 1995). In contrast, in Spain any rent extraction usually occurs between majority and minority shareholders—the so-called tunneling effect (Johnson et al., 2000)—due to the presence of a few dominant owners with significant stable shareholdings (De Miguel et al., 2004; Salas, 2002). Although the majority shareholders in Spain are motivated to monitor the actions of executives, they themselves also usually serve as executive directors, thereby gaining the opportunity to negotiate agreements with the other members of the board, making decisions that will benefit themselves regardless of the interests of the minority shareholders (Baixauli-Soler & Sánchez-Marín, 2011, 2015). Thus, the UK firms are characterized by a dispersed form of control whose main agency conflict is the classic principal–agent type, while in Spain, there is a much more concentrated form of control resulting in a principal–principal agency conflict (Morck et al., 2005; Young et al., 2008).

Another aspect that differentiates these two countries is the degree of shareholder protection. The United Kingdom has a legal system that follows a common-law tradition while Spain has a civil-law legal system. Consequently, the United Kingdom is characterized by strong protection of minority shareholders and high levels of transparency and mandatory disclosure of information by firms (Kirkbride & Letza, 2009). In contrast, Spain has relatively weak protection of minority shareholders and less transparency in the information published by firms (Leech & Manjon, 2002). In this sense, some studies show that the legal system derives largely from the type of ownership structure prevalent in a country. This is generally because countries with dispersed ownership structures tend to have a more protective system than countries with more concentrated ownership (La Porta et al., 1999). In Spain, this peculiarity can only encourage the principal–principal conflict because minority shareholders lack legal protection and this makes it difficult to counter any opportunistic behavior on the part of the controlling shareholders. Thus, expropriation tends to be higher in countries with concentrated ownership and lower investor protection, as is characteristic of Spain (Salas, 2002).

Additionally, the degree of the capital market development helps explain some other differences of corporate governance systems. The functioning of the market for corporate control as an effective discipline mechanism requires capital market liquidity (Leech & Manjon, 2002). In a liquid capital market, if incumbent shareholders or potential owners perceive that executives are not managing a firm efficiently, they can carry out a transfer of control variously through acquisitions, mergers or other third-party transactions, thereby replacing the current top management team (La Porta et al., 1998). The capital market in the United Kingdom is substantially more liquid and developed than in Spain. This favors the market for corporate control as an effective external control mechanism in the United Kingdom, because transfer of control to other executives is easier to bring about, thereby complementing the existing internal monitoring mechanisms (Weir et al., 2002). In contrast, the less developed capital market in Spain means that the monitoring function relies exclusively on the internal mechanisms that play a role in the supervision of executives (Sánchez-Marín et al., 2011). Furthermore, this capital market situation in Spain is detrimental to the minority shareholders should they decide to sell their holdings when they perceive they are being abused by the majority. This, in turn, increases the possibility of expropriation and intensifies the principal–principal conflict in Spain (Johnson et al., 2000).

Thus, the significant differences between the United Kingdom and Spain in terms of the context of corporate governance are clear. The more dispersed control, with greater legal protection of minorities, and a more developed market for corporate control as found in the United Kingdom, contrasts with the more concentrated control, the lower legal shareholder protection, and the less liquid capital market of Spain. Consequently, we can also expect different degrees of effectiveness in the governance mechanisms (ownership structure and board of directors) that monitor the degree of alignment of executive compensation. We analyze these mechanisms and their relationships with executive compensation in the following sections.

2.2 | Ownership structure and executive compensation

Reflecting the balance between the preferences of owners and managers, ownership structure is a natural mechanism for monitoring executives (Morck et al., 1988, 2005). Specifically, ownership concentration, proportion of shares owned by directors, and institutional ownership are three of the main elements that characterize the efficiency of ownership structure as a mechanism of executive compensation monitoring (Cosh & Hughes, 1997; Mehran, 1995; Werner et al., 2005).

Agency theory predicts that when ownership is dispersed, individual owners have weak incentives to influence on corporate decision as well as to invest in executive monitoring (Fama & Jensen, 1983; Jensen & Meckling, 1976). This free rider problem may be mitigated by concentrated share ownership (Conyon & He, 2011). A more concentrated ownership structure enables greater monitoring of executives because large, dominant shareholders are more motivated to discipline executives through a design of compensation that guides their decision making towards maximizing the shareholders' interests, namely, firm performance (Tosi & Gomez-Mejia, 1994; Werner et al., 2005). This effect is well known as the alignment hypothesis, which implies a strong incentive of dominant owners to monitor executives, mitigating their potential entrenchment, which is positively associated with high compensation alignment with the firm performance, as a way to maximize company value (Carpenter & Sanders, 2002; Sánchez-Marín et al., 2017).

However, although concentrated ownership can help mitigate the principal–agent problem, it can also increase the principal–principal conflict (Faccio & Lang, 2002; Thomsen et al., 2006). Set against the beneficial effects of concentrated ownership are the costs associated with entrenchment and private benefits of control of large shareholders linked to the management (executives), the governance (directors), or both simultaneously (Faccio et al., 2001; Shleifer & Vishny, 1997). Large shareholders may exploit their power to expropriate minority shareholders or promote their own objectives over those of other shareholders. This potential appropriation of private benefits may occur via tunneling or rent extraction strategies (La Porta et al., 2002) which include those linked to excess executive compensation practices (Baixauli-Soler & Sánchez-Marín, 2015).

The type of ownership is also important. Institutional investors constitute an organized group—banks, pension funds, insurance companies, and investment societies—which characteristically holds a long-term portfolio of investments in firms and whose objective is the maximization of firm value (Hartzell & Starks, 2003). Institutional investors take the role of traditional owners and exercise stricter control over executives and their compensation (Cheng & Firth, 2005; David et al., 1998), reducing both executive discretion and potential agency problems. They can remove incentives for passivity of minority shareholders, having the ability to directly monitor executives promoting aligned executive compensation packages and minimizing thus excess payments (Cheng & Firth, 2005).

How can we characterize the ownership structure of listed firms in the United Kingdom and Spain? Considering past evidence, ownership in the UK firms has long been widely dispersed, and this situation is also recognized as creating a control problem (Mayer, 2013). This *principal–agent* conflict manifests itself through shareholders having less incentive to monitor managerial decisions, provided they continue to receive sufficient dividends (Grossman & Hart, 1980; Maug, 1998). Faced with the prospect of having to incur high transaction costs in actively monitoring management, and with only a modest claim on any benefits resulting from such monitoring, shareholders usually take a passive attitude in defense of their interests by delegating their vote to the board. This action consequently increases the power of executives, leading to a possible expropriation of rents because of the executives' greater discretion to set their own pay (Bebchuk et al., 2002). In this vein, Short and Keasey (1999) and Weir et al. (2002) demonstrate that the percentage of ownership by executives has remained around 10%, while Ozkan (2011) shows an increase in external ownership with large institutional shareholders having around 30%, with the remaining stake in the hands of minority shareholders (60%). Although the United Kingdom gives minority shareholders special protections—for example, pre-emption rights, essentially the right of existing shareholders to first refusal on new share issues, a right that is not available in other capital markets—it seems that such investors are inclined towards a diversified portfolio strategy (Franks et al., 2009), further highlighting the principal–agent conflict.

Studies examining the relationship between ownership structure and executive compensation focus primarily on institutional investors, as these investors have the potential power to align executive compensation. However, Cosh and Hughes (1997), analyzing a set of UK firms during the period 1989–1994, suggest that the presence of institutional investors has no significant impact on the alignment of executive compensation. On the other hand, Ozkan (2011) studies a set of non-financial firms listed on the UK stock market and finds that the presence of institutional ownership and block-holder ownership has a generally positive impact on the efficiency of executive compensation. However, Ozkan (2011) also evidences a dark side, finding that when the level of executives' ownership is higher, their alignment of compensation is lower.

Spanish listed firms are characterized by a high concentration of ownership and a high number of cross-shareholdings (De Miguel et al., 2004; La Porta et al., 1999). Several studies provide evidence of a *principal–principal conflict*, as approximately 90% of Spanish firms are under majority control with the largest shareholder reaching almost 40% of the direct shares and 50% of indirect shares[1] (Baixauli-Soler & Sánchez-Marín, 2011; Baixauli-Soler & Sánchez-Marín, 2015; Salas, 2002). Such majority owners usually manage the firm directly (as executive directors). This leaves the remaining stake in the hands of institutional investors (between 10% and 20%) and minority shareholders (around 40%). In addition, there exists a large number of crossholdings of shares in Spain—more than 40% of listed firms have significant crossholdings of shares. This means that some shareholders may be present in the multiple roles of executive director and majority shareholder (Baixauli-Soler & Sánchez-Marín, 2011). They are,

thereby, able to exploit their position to expropriate (via tunneling) substantial income from the minority shareholders (Johnson et al., 2000).

Several studies have explained how these structural aspects of ownership influence executive compensation. Sánchez-Marín et al. (2011) finds, in a sample of listed firms over the years 2004–2007, that the relationship between executive share ownership and compensation is dominated by the entrenchment effect: majority shareholders usually also assume the role of executives, with their compensation being excessively high and poorly aligned to firm performance. Similarly, Baixauli-Soler and Sánchez-Marín (2011) analyze a set of Spanish listed firms during the period 2003–2007, showing that executive compensation is only slightly sensitive to changes in the firm's economic situation owing to the ownership concentration being in the hands of internal controlling shareholders (executive directors). Furthermore, Baixauli-Soler and Sánchez-Marín (2015), using a sample of listed firms over the period 2004–2012, corroborate the inefficient compensation of executives as arising from the persistent low proportion of dispersed ownership and the absence of significant institutional investors.

Taking into account all the above arguments, and consistent with agency theory, we expect the ownership structure of the UK listed firms—more favorable to concentrated ownership in the hands of institutional investors and with high level of protection of minorities—will be more associated with the design of optimal executive compensation alignment (being more linked to company performance) in comparison with the ownership structure of Spanish firms—more concentrated in large shareholders occupying key positions in the firms (either as a director or as a manager), with low level of minority shareholders protection. In other words, we expect higher excess executive compensation in Spain than in the United Kingdom due to the less efficient ownership structure as a mechanism of monitoring. Formally stated:

> **H1a.** : Ownership concentration and proportion of ownership in the hands of outside directors and institutional investors are positively related to executive compensation alignment.

> **H1b.** : Corporate governance context significantly moderates the relationship between ownership structure and executive compensation alignment: UK firms' ownership structure is more effective than that of the Spanish firms for designing aligned executive compensation.

2.3 | Board of directors and executive compensation

The board of directors seeks to align the interests of executives and shareholders both directly through the monitoring of executive actions and indirectly through the design of a pay-for-performance system for executive pay (Chatterjee et al., 2003). The literature reveals that aspects related to the size, composition, and structure of the board, in terms of functioning, coordination, and degree of independence, are those most closely associated with the effectiveness of the monitoring of executives (Adams et al., 2010; Conyon & Peck, 1998).

Specifically, previous research argues that independent (outside) directors have more incentives to effectively monitor the executives because they are less subject to executives influence and have reputations to protect in the labor market (Core et al., 1999; Fama & Jensen, 1983). Executives—and the CEO—can exert larger influence over inside directors since they are usually more loyal to them and, in addition, can be controlled by such factors as their career opportunities. We thus expect more independent directors on the board are associated with less managerial opportunism and more efficient compensation contracts (Conyon & He, 2011). In addition, previous research points out that board effectiveness is influenced by its size (Cyert et al., 2002; Yermack, 1996): Large boards are less effective than small boards, because they may suffer from free-riding problems in decision making and control thereby diluting executive monitoring abilities (Brick et al., 2006; Sánchez-Marín et al., 2010; Sapp, 2008). Similarly, boards that combine CEO and chairperson positions in a single person (in the so-called duality structure of leadership) vest more power with the executives, and may suffer greater agency costs (Jensen, 1993), being less effective at setting executive pay (Boyd, 1994; Chhaochharia & Grinstein, 2009). Thus, it is expected that these differences in board characteristics will ultimately determine the relative efficiency of executive compensation when comparing the United Kingdom and Spain.

In the context of UK firms, Weir et al. (2002) analyze boards and find that independent directors represent 42% of the board. In terms of the power structure, UK boards are relatively independent as compared with other countries. For example, only in 16% of firms does the position of CEO and Chair of the board coincide ("duality"). Bonet and Conyon (2005) show that the typical size of the board in the United Kingdom is seven members. Ozkan (2011) demonstrates that the size of the boards has increased slightly to eight members and that the presence of non-executive directors is around 57%. For 100 completed M&A bids in the United Kingdom over the 1998–2001 period, Coakley and Iliopoulou (2006) find that larger boards with fewer independent directors award significantly higher bonuses and salaries post M&A. However, for a sample of 414 UK firms in 2003, Ozkan (2007) finds that the proportion of non-executive directors has a positive impact on executive compensation, suggesting that non-executive directors do not, in fact, play a monitoring role. In a subsequent paper, Ozkan (2011) confirms this finding, showing that a higher proportion of independent directors is associated with higher total executive compensation in poorly performing firms, while nevertheless revealing a positive relationship between independent directors and pay-for-performance. Finally, Gregory-Smith and Main (2015) show this positive association discussion in terms of a legitimacy effect imparted by the presence of non-executive directors.

The boards of directors of Spanish show a stable average size of 11 members, revealing a composition of 25% of executive directors while the remaining 75% are external, of which only 35% are classified as independents (Salas, 2002; Sánchez-Marín et al., 2010). In terms of the structure of power, more than 60% of firms combine the Chair of the board with the position of CEO—"duality" (Sánchez-Marín et al., 2010, 2011). Studies examining the influence of the board on the compensation of directors in Spanish listed firms arrive at a range of findings. For example, Sánchez-Marín et al. (2010) find that for the period 2004–2006 when the total number of directors is lower, a higher proportion of independents is associated with executive compensation that is both lower and more strongly linked to firm performance. Furthermore, Baixauli-Soler and Sánchez-Marín (2011) show that the board slightly moderates the ability to adjust the executive compensation to changes in internal and external factors of the firm. Specifically, although the presence of independent directors generally aligns executive compensation, those boards with duality are associated with significantly higher fixed salary and misaligned total compensation. Ultimately, Baixauli-Soler and Sánchez-Marín (2015) show that the characteristics of Spanish boards do not have any significant influence on the fixed or variable compensation of executives in those firms controlled by internal shareholders (executive directors), a situation which characterizes the majority of Spanish listed firms.

Considering all these arguments and in line with agency theory, we expect that UK firms' boards, with more appropriate characteristics regarding supervisory effectiveness—smaller-tight size, greater proportion of independent directors, and the presence of non-dual power structures—in comparison with those of the Spanish firms' boards, to have a positive effect on the design of more optimal executive compensation package (more directly linked with company performance). In other words, we hypothesize that Spanish firms will have higher excess executive compensation than UK firms due to the less efficient boards monitoring. Formally stated

> **H2a.** : Small board size, proportion of independent directors on board, and non-dual structures of board leadership are positively related to executive compensation alignment.

> **H2b.** : Corporate governance context significantly moderates the relationship between board characteristics and executive compensation alignment: UK firms' boards are more effective than those of the Spanish firms for designing aligned executive compensation.

3 | METHODOLOGY

3.1 | Data

The sample comprises 260 non-financial firms listed on the stock exchanges of either the United Kingdom or Spain during the period 2005–2012. Specifically, 166 firms are from the United Kingdom, and 94 firms are from Spain. This results in a total numbers of 1893 firm-year observations. Financial firms have been excluded due to differences in regulation and in the format of their annual accounts. The information regarding executive compensation and corporate governance of the UK firms was obtained from a proprietary database supplied by Manifest Ltd. Financial data are derived from DataStream. The compensation and governance data of Spanish firms have been gathered by hand from the annual corporate governance reports published by the Spanish Securities Market Commission (CNMV). The financial information for these firms was obtained from the Osiris database (Bureau Van Dyck Electronic Publishing). Macroeconomic variables are taken from World Bank Cross-Country Data. We have converted the financial data from euros to pounds sterling using the annual average spot exchange rate. We have also converted data to 2010 values using the respective UK and Spanish price index deflators.

3.2 | Variables

3.2.1 | Excess executive compensation

The compensation of executives is measured as recommended in the literature (Carpenter & Sanders, 2002; Core et al., 1999; Tosi et al., 2000). This covers the average amount received by the top management team (CEO and executive directors) and encompasses the following components: fixed salary, short-term incentives, and long-term incentives. Specifically, based on these measures we construct two variables: (1) *executive total compensation* (TOTAL_COMP), measured as the sum of fixed salary, variable cash compensation, and value of stock options plans granted during the year; and (2) *executive cash compensation* (CASH_COMP) calculated as sum of fixed salary and variable cash compensation.

We use these to compute TOTAL_ALIG and CASH_ALIG that are measures of expected or efficient executive compensation that reflect the alignment of the executive compensation to the performance of the firm. We calculate efficient compensation by regressing the compensation (total and cash) on firm- and year-specific outcome measures of the economic determinants of executive compensation according to the model (Core et al., 1999; Core et al., 2008):

$$TOTAL\_ALIG_{it} = \beta_0 + \beta_1 \cdot ln(SIZE_{it-1}) + \beta_2 \cdot ROA_{it} + \beta_3 \cdot ROA_{it-1} + \beta_4 \cdot RET_{it} + \beta_5 \cdot RET_{it-1} + \beta_6 \cdot BTM_{it-1} + n_i + d_t + \psi_i + e_{it}$$

(1)

Here, t is the year that the executive compensation is paid. The dependent variable is the natural log of total compensation, measured respectively as total and cash compensation (TOTAL_COMP and CASH_COMP) at the end of the year t. The size of the firm is measured over the prior year. ROA is measured as income before extraordinary items divided by total assets for the prior and current year

respectively. Stock return (RET) is the shareholder return at the end of the year. The book to market (BTM) measure is calculated as the market value of equity plus the book value of debt divided by book value of assets. ψ_t, η_i, and ε_{it} are the time effects, the unobserved individual heterogeneity and the error term, respectively. Year indicators and industry variables are also included. We estimate this regression model using a system GMM methodology, estimating the efficient or expected executive compensation by exponentiation the expected value of this equation (producing TOTAL_ALIG and CASH_ALIG, respectively).

Following Core et al. (2008) and Brunarski et al. (2015), we use estimated excess executive compensation as our dependent variable. This measure is an indicator of the deviation of executive compensation from what might be expected given the respective firm's performance (Alissa, 2015; Ferri & Maber, 2013). Excess executive total compensation (EETC) and excess executive cash compensation (EECC) are calculated as the logarithm of executive director excess compensation—using total compensation (TOTAL_COMP) and cash compensation (CASH_COMP) divided by aligned compensation—total aligned compensation (TOTAL_ALIG) and cash aligned compensation (CASH_ALIG), respectively, as model of Alissa (2015) and Sánchez-Marín et al. (2017).

$$EETC_{it} = \ln\left(\frac{TOTAL\_COMP_{it}}{TOTAL\_ALIG_{it}}\right)$$

$$EECC_{it} = \ln\left(\frac{CASH\_COMP_{it}}{CASH\_ALIG_{it}}\right)$$

3.2.2 | Ownership structure

Ownership structure has been operationalized through three variables (Cyert et al., 2002; Werner et al., 2005): (1) board ownership (DIROW), defined as the average percentage of ownership in the hands of directors (Mehran, 1995); (2) institutional ownership (INSOW), measured as the average proportion of ownership in the hands of institutional investors (Bushee, 1998); and (3) ownership concentration (HERFIN), through the Herfindahl index of ownership concentration (Himmelberg et al., 1999), that is, the sum of the squares of the market shares of the largest shareholders expressed as fractions, which ranges from 0 to 1 as one moves from dispersed ownership to concentrated ownership.

3.2.3 | Board characteristics

The effectiveness of the level of monitoring by the board of directors is captured in three variables (Boyd, 1994; Coles et al., 2008; Conyon & Peck, 1998; Daily et al., 1998): (1) the size of board of directors, measured by the logarithm of the number of directors (LNDIR); (2) the proportion of independent directors (PIND), measured

as the number of independent directors divided by the total number of directors on the board; and (3) duality (DUAL), which captures the duality on the board through a dummy variable which takes the value 1 when the same person occupies the roles of CEO and Chair of the board, and 0 otherwise.

3.2.4 | Control variables

We have included seven control variables which have a direct bearing on expected executive compensation (Gomez-Mejia & Wiseman, 1997; Tosi et al., 2000): (1) return on assets (ROA), measured by dividing net income by total assets; (2) growth opportunities (Q), measured by the Tobin's Q measure of the market value of equity plus the book value of debt divided by book value of assets; (3) firm size (SIZE), calculated as the logarithm of the number of employees; (4) firm age (AGE), measured as the number of years since the company was founded; (5) financial leverage (FL), measured as the ratio of total debt to total assets; (4) gross domestic product (GDP) growth calculated as annual percentage growth rate of GDP at market prices based on constant local currency; and (5) industry, included through nine dummy variables representing the specific economic sectors to which firms belong: BASMAT (basic materials), HEALTH (healthcare), INDUST (industrial), CONGDS (consumer goods), TECH (technology), UTIL (utility industry), OILGAS (oil and energy), CONSER (construction), TELECO (telecommunications).

3.3 | Models' specifications

First, we have specified the following econometric models for each compensation variable. Equations (1) and (1′):

$$EETC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (1)$$

$$EECC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (1')$$

where ETTC and EECC represent EETC and EECC, respectively. UK is a dummy variable that takes value one when is a UK firm and zero when is a Spanish firm. In this way, if β_0 is positive (negative), it indicates that excess compensation in UK firms is higher (lower) on average than in the Spanish firms. We control for macroeconomic and firm characteristics, $CONTROL_{i,t}$: return on assets, Tobin's Q, size, age, financial leverage, GDP growth, and industry. The data are adjusted to control for inflation and exchange rate fluctuations. Finally, ψ_t, η_i, and ε_{it} are the time effects, the unobserved individual heterogeneity, and the error term, respectively.

In the following models, we estimate Equations (2) and (2′), which includes $OWNERSHIP_{i,t}$: ownership of executive directors, ownership of institutional investors, and ownership concentration.

$$EETC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot OWNERSHIP_{i,t} + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (2)$$

$$EECC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot OWNERSHIP_{i,t} + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (2')$$

Next, we include the influence of board characteristics, through Equation (3) and (3').

$$EETC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + + \sum \beta \cdot BOARD_{i,t} + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (3)$$

$$EECC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot BOARD_{i,t} + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (3')$$

In Equations (3) and (3'), we include the board variables previously described, $BOARD_{i,t}$: the percentage of independent directors, the presence of duality, and the logarithm of the number of directors on the board.

To analyze the moderating effect of the country on the ownership structure, we include the following models:

$$EETC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot UKOWNERSHIP_{i,t} + \sum \beta \cdot OWNERSHIP_{i,t} + + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (4)$$

$$EECC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot UKOWNERSHIP_{i,t} + \sum \beta \cdot OWNERSHIP_{i,t} + + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (4')$$

where, UKOWNERSHIP is calculated as the UK dummy variable multiplied by the $OWNERSHIP_{i,t}$ variable.

Finally, we propose the models Equations (5) and (5') as follows:

$$EETC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot UKBOARD_{i,t} + \sum \beta \cdot BOARD_{i,t} + + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (5)$$

$$EECC_{i,t} = \alpha + \beta_0 \cdot UK_{i,t} + \sum \beta \cdot UKBOARD_{i,t} + \sum \beta \cdot BOARD_{i,t} + + \sum \beta \cdot CONTROL_{i,t} + \psi_t + \eta_i + \varepsilon_{it} \quad (5')$$

where UKBOARD comprises the UK dummy variable multiplied by $BOARD_{i,t}$.

These equations are estimated using a panel data methodology, applying the System GMM technique (Arellano & Bover, 1995; Blundell & Bond, 1998). This methodology makes it possible to control for individual heterogeneity, introducing an individual effect, η_i. In addition, GMM estimation system solves the endogeneity problem

with the estimation of a system of two simultaneous equations, one equation in levels (with lagged first differences instruments) and the other in first differences (with lagged level instruments). We used lagged variables as instruments to control for the persistence over time of the variables relating to the ownership and board of directors. Indeed, specific corporate governance studies such as those of Wintoki et al. (2012) or Schultz et al. (2010) illustrate that GMM specifications are quite valid to be applied in panels focused on comprehensive analysis of the governance–performance relationships that also recognizes that multiple agency conflicts requiring simultaneous management exist within a firm. In addition, Sargan Test complement our GMM analyses helping us to verify the absence of over-identifying restrictions of the models.

4 | RESULTS

Table 1 reports the descriptive statistics relating to excess compensation and the governance characteristics for the full sample and for UK and Spanish firms separately. In general, the firms are different in terms of all the variables analyzed. Specifically, we observe lower excess in compensation in the UK firms than in Spanish firms. Regarding governance characteristics, there is a higher proportion of independent directors and higher mean level of ownership in the hands of executive directors, as well as higher board size, greater prevalence of duality and a higher ownership concentration in the Spanish firms than in UK ones. Finally, firms in the UK are characterized by higher institutional ownership, stronger firm performance, greater firm growth opportunities, and higher economic country growth than in Spain.

As can be seen in Table 2, although a high correlation is observed between control variables (size and performance or performance and concentration), most values are clearly acceptable in terms of multicollinearity and do not raise problems for the interpretation of the results, as all values of VIF are below 10 (with specific values as follows: mean: 3.14; median: 2.78; max: 7.76; min: 2.65; SD: 1.26).

Table 3 shows the differences in excess compensation between UK and Spanish firms taking into account the main institutional characteristics that can explain compensation, Equations (1) and (1'). We observe a negative effect of the UK dummy variable on EETC and on EECC. The results indicate lower excess compensation in the UK firms than in Spanish ones. Moreover, firm size, firm performance, firm age, are positively related to excess executive compensation while financial leverage and opportunities for growth have a significant and negative effect on excess executive compensation.

Table 4 shows the influence of ownership structure on excess executive compensation measured in terms of both total (Models 1 to 4) and cash (Models 5 to 8) compensation. We find, consistent with the evidence in Table 3, that excess executive compensation in UK firms is lower than in Spanish firms. In addition, results indicate that the percentage of shares owned by directors, the proportion of institutional ownership and the ownership concentration have the effect of increasing excess executive compensation. The influence of both

TABLE 1 Descriptive statistics

	All firms				UK firms				Spanish firms			
	Mean	SD	Min.	Max.	Mean	SD	Min.	Max.	Mean	SD	Min.	Max.
Executive compensation												
EETC	0.011	0.851	−4.181	2.908	0.015	0.665	−1.914	1.971	0.031	1.511	−4.181	2.908
EECC	−0.006	0.819	−3.996	3.150	−0.083	0.574	−0.096	1.686	0.156	1.165	−3.996	1.165
Ownership structure												
DIROW	15.742	20.098	0.000	99.497	9.407	11.461	0.000	75.606	26.325	26.092	0.000	99.497
INSOW	34.496	21.988	0.000	100.000	41.977	16.989	0.000	97.256	22.014	23.660	0.000	100.000
HERFIN	0.063	0.146	0.000	1.000	0.006	0.026	0.000	1.000	0.160	0.203	0.000	1.000
Board characteristics												
PIND	22.527	17.840	0.000	88.88	16.551	15.431	0.000	75.000	32.497	17.125	0.000	88.888
DUAL	0.255	0.436	0.000	1.000	0.056	0.231	0.000	1.000	0.587	0.492	0.000	1.000
LNDIR	2.183	0.331	0.693	3.178	2.082	0.291	0.693	3.044	2.352	0.326	1.386	3.178
Control variables												
ROA	4.222	7.846	−27.220	33.400	6.735	9.036	−27.220	33.400	3.200	11.900	−89.406	144.310
Q	2.278	3.675	−21.120	23.466	2.405	4.256	−21.120	33.400	2.067	2.402	0.000	23.446
SIZE	7.086	14.578	0.693	7.96	7.983	1.409	2.995	19.510	5.579	2.125	0.693	13.379
AGE	9.166	0.753	6.068	11.036	8.982	0.614	6.630	9.771	9.445	0.853	6.068	11.036
FL	0.359	0.787	0.000	26.138	0.202	0.175	0.000	1.331	0.597	1.191	0.000	26.138
GDP	0.686	2.675	−4.200	−4.200	1.000	2.205	−4.200	3.100	0.201	3.202	−3.600	4.200
BASMAT	0.082	0.275	0.000	1.000	0.066	0.249	0.000	1.000	0.109	0.312	0.000	1.000
HEALTH	0.037	0.189	0.000	1.000	0.038	0.193	0.000	1.000	0.034	0.183	0.000	1.000
INDUST	0.322	0.467	0.000	1.000	0.422	0.494	0.000	1.000	0.157	0.364	0.000	1.000
CONGDS	0.120	0.325	0.000	1.000	0.116	0.321	0.000	1.000	0.126	0.332	0.000	1.000
TECH	0.065	0.248	0.000	1.000	0.083	0.276	0.000	1.000	0.037	0.188	0.000	1.000
UTIL	0.014	0.198	0.000	1.000	0.016	0.128	0.000	1.000	0.082	0.274	0.000	1.000
OILGAS	0.045	0.209	0.000	1.000	0.050	0.218	0.000	1.000	0.039	0.194	0.000	1.000
CONSER	0.248	0.432	0.000	1.000	0.194	0.395	0.000	1.000	0.338	0.473	0.000	1.000
TELECO	0.035	0.184	0.000	1.000	0.011	0.104	0.000	1.000	0.075	0.263	0.000	1.000

Notes: EETC, excess of executive total compensation; EECC, excess of executive cash compensation; PIND, percentage of independent directors on the board; DUAL, percentage of firm with duality of CEO and Chair; LNDIR, logarithm of the number of directors; DIROWN, percentage of executives' ownership; INSOWN, percentage of institutional investors' ownership; HERFIN, Herfindahl index of ownership concentration; ROA, return on assets; Q, Tobin's Q; SIZE, firm size measured by the logarithm of number of employees; AGE, firm age measured by the logarithm of the number of days; FL, financial leverage measured as the ratio of total debt to total assets; GDP, annual GDP growth; BASMAT, dummy that takes a value of one if the firm belongs to the basic materials industry and zero otherwise; HEALTH, dummy that takes a value of one if the firm belongs to the healthcare industry and zero otherwise; INDUST, dummy that takes a value of one if the firm belongs to the industrial industry and zero otherwise; CONGDS, dummy that takes a value of one if the firm belongs to the consumer goods industry and zero otherwise; TECH, dummy that takes a value of one if the firm belongs to the technology industry and zero otherwise; UTIL, dummy that takes a value of one if the firm belongs to the utility industry and zero otherwise; OILGAS, dummy that takes a value of one if the firm belongs to the oil and energy industry and zero otherwise; CONSER, dummy that takes the a of one if the firm belongs to the construction industry and zero otherwise; TELECO, dummy that takes a value of one if the firm belongs to the telecommunications industry and zero otherwise.

TABLE 2 Correlations

Variable	1	2	3	4	5	6	7	8	9	10	11	12	13
1. EETC	1.000												
2. EECC	.935	1.000											
3. PIND	−.044	.041	1.000										
4. DUAL	.098	.214	.316	1.000									
5. LNDIR	.426	.474	.182	.272	1.000								
6. DIROWN	−.201	−.121	.123	.289	.078	1.000							
7. INSOWN	.021	−.037	−.157	−.230	−.209	−.320	1.000						
8. HERFIN	.094	.177	.207	.261	.231	.187	−.125	1.000					
9. ROA	.107	.076	−.164	−.221	−.131	−.162	.115	−.216	1.000				
1. Q	.056	.039	−.004	−.030	−.016	.000	−.003	−.036	.164	1.000			
11. SIZE	.313	.235	−.336	−.309	−.015	−.362	.141	−.273	.304	.005	1.000		
12. AGE	.124	.183	.117	.238	.251	.106	−.211	.198	−.150	−.006	−.105	1.000	
13. FL	.092	.170	.180	.327	.342	.260	−.314	.335	−.269	−.080	−.174	.358	1.000
14. GDP	.007	−.029	−.046	−.104	−.077	−.074	−.015	−.087	.157	.066	.088	−.102	−.156
15. UK	.006	−.137	−.444	−.584	−.411	−.424	.410	−.531	.406	.040	.569	−.396	−.620
16. BASMAT	−.080	−.058	.055	.074	.050	.027	−.047	.014	.004	.044	−.032	.116	.035
17. HEALTH	−.033	−.040	−.01	.068	−.093	.007	−.063	−.035	−.096	.015	−.084	−.045	−.031
18. INDUST	−.098	−.149	−.195	−.196	−.246	−.122	.118	−.146	.165	−.021	.161	.017	−.180
19. CONGDS	−.054	−.047	−.017	.001	−.038	.050	−.064	−.034	−.025	.020	−.078	−.040	−.059
20. TECH	.022	−.010	.065	.054	−.073	−.064	.073	−.050	−.069	.037	−.067	−.072	−.101
21. UTIL	.093	.120	.042	.057	.149	−.056	−.083	.171	−.050	.005	.042	.010	.121
22. OILGAS	.117	.109	.019	−.024	.118	−.026	.027	−.009	.033	.011	−.010	.065	−.036
23. CONSER	.081	.115	.093	.081	.168	.158	.014	.137	−.051	−.047	.012	−.045	.224
24. TELECO	.073	.118	.122	.041	.172	−.013	−.135	.054	−.068	−.023	−.117	.023	.099

TABLE 2 (Continued)

Variable	14	15	16	17	18	19	20	21	22	23	24
1. EETC											
2. EECC											
3. PIND											
4. DUAL											
5. LNDIR											
6. DIROWN											
7. INSOWN											
8. HERFIN											
9. ROA											
1. Q											
11. SIZE											
12. AGE											
13. FL											
14. GDP	1.000										
15. UK	.160	1.000									
16. BASMAT	−.008	−.082	1.000								
17. HEALTH	−.016	−.020	−.058	1.000							
18. INDUST	.063	.284	−.216	−.147	1.000						
19. CONGDS	−.011	−.056	−.113	−.077	−.284	1.000					
20. TECH	.014	.040	−.075	−.051	−.189	−.099	1.000				
21. UTIL	−.032	−.125	−.055	−.037	−.139	−.072	−.048	1.000			
22. OILGAS	.004	−.003	−.061	−.041	−.153	−.080	−.053	−.039	1.000		
23. CONSER	−.028	−.108	−.160	−.109	−.402	−.210	−.140	−.103	−.114	1.000	
24. TELECO	−.039	−.178	−.054	−.036	−.135	−.071	−.047	−.034	−.038	−.100	1.000

TABLE 3 System GMM regressions on excess of executive compensation

Variable	EETC	EECC
UK	$-.413^{***}$ (-6.44)	$-.631^{***}$ (-10.20)
Control variables		
SIZE	$.189^{***}$ (16.17)	$.180^{***}$ (18.85)
ROA	$.011^{***}$ (11.90)	$.015^{***}$ (17.55)
AGE	$.293^{***}$ (10.79)	$.221^{***}$ (10.43)
FL	$-.391^{***}$ (-7.48)	$-.360^{***}$ (-8.63)
Q	$.003^{***}$ (3.87)	$-.005$ (0.67)
GPD	$-.004^{**}$ (-2.14)	$-.002^{***}$ (-9.02)
CONS	-4.532^{***} (-16.31)	-3.364^{***} (-16.75)
Industry dummies	Yes	Yes
Year dummies	Yes	Yes
Tests		
F	74.47^{***}	75.07^{***}
z_1	.000	.000
z_2	.000	.000
Sargan	.564	.659

Notes: T statistic in parentheses. *F* statistic (test of combined significance); z_1 and z_2 are two Wald tests of the joint significance of the reported coefficients and the joint significance of the time dummy variables, respectively (asymptotically distributed as λ^2 under the null hypothesis of no relationship, probability is shown); Sargan is a test of the over-identifying restrictions, asymptotically distributed as λ^2 under the null hypothesis of no correlation between the instruments and the error term, probability is shown.
***Significance at 1% level.
**Significance at 5% level.
*Significance at 10% level.

ownership concentration and directors ownership offers support for the entrenchment hypothesis, that consider ownership concentration in the hands of insiders as a factor that facilitates executives pursuing their own interests emphasizing executives rents appropriation via excess compensation. These findings confirm the dominance of the principal–principal conflicts (Faccio & Lang, 2002; Thomsen et al., 2006), whereby a majority shareholder uses his/her power to extract private benefits, taking into account neither the firm's nor the minority shareholders' interests (Faccio et al., 2001; Shleifer & Vishny, 1997) using compensation as a way of sharing such benefits with executives. Contrary to our expectations, the positive influence of institutional investors in excess executive compensation can be explained by the higher influence of executives and insider directors to take priority over shareholders' interests as well as the fewer incentives of institutional to monitoring executives due to the well diversification of their investments (Pound, 1988).

Table 5 analyzes the effect of board characteristics on excess executive compensation. According to our expectations, the proportion of independent directors reduce both excess executive total (Models 1 to 4) and cash (Models 5 to 8) compensation. This result supports the agency view that more effective supervision results in a

more effective design of executive compensation packages (Brick et al., 2006; Sapp, 2008). We also find that excess executive compensation rises in the presence of the duality of CEO and chairman. Of course, the concentration of power in one single person occupying CEO and chairman positions vests more discretion to executives, being less effective at setting proper alignment of executive compensation (Chhaochharia & Grinstein, 2009; Donaldson & Davis, 1991). Finally, in large boards, the excess executive compensation is higher. This finding is consistent with the view that both agency and coordination/communication problems become more severe as a board grows larger (Caspar, 2005; Lipton & Lorsch, 1992; Song & Windram, 2004).

Table 6 investigates the moderating effect of country (United Kingdom vs. Spain) on the ownership structure in explaining excess executive compensation. We find that in the United Kingdom, a higher proportion of shares owned by the directors is more effective in reducing excess executive compensation, supporting the alignment hypothesis (Fama & Jensen, 1983). We also find that, among UK firms, an increase in institutional ownership reduces excess executive compensation. In the United Kingdom, institutional investors tend to exert greater control on corporate supervision due to (1) economies of scale and the higher liquidity of the UK capital market and (2) the more experience when it comes to exercising control at a lower cost (Pound, 1988). Finally, we find that ownership concentration is also more effective in the United Kingdom than in Spain in terms of reducing opportunistic behavior on the part of insiders, which can be explained by more favorable the strong presence of institutional investors in the ownership of UK firms, which results in closer executive monitoring in terms of compensation.

Finally, the moderating effect of country on board characteristics is reported in Table 7. The interaction between the country dummy variable, United Kingdom, and the percentage of independent directors indicates that board independence is more effective in the United Kingdom in terms of limiting excess executive compensation. On the other hand, board size seems to be associated with laxer executive pay outcomes than in Spain. The strongest result is regarding duality: despite the presence of duality on boards theoretically increase agency costs as this concentration of power allows executives to pursue their own self-interest (Conyon & Peck, 1998), we find that in the United Kingdom, either because the practice is relatively rare or dominant shareholders tend to use in these infrequent cases their power to compensate this structure of power (Abels & Martelli, 2013), the impact on excess executive pay is significantly less as compared to this of the Spanish firms.

We additionally conduct a propensity score matching (PSM) analysis to confirm the absence of potential endogeneity in the above GMM estimations and, therefore, the robustness of our findings. For each year, firms in United Kingdom are considered as the treated group, and Spanish firms are used as a control group. The treated and control samples are pooled across all years to estimate the propensity score as a function of firm control variables as a matching ones: firm size, return on assets, firm age, financial leverage, Tobin's Q, and annual GDP growth. Table 8 shows the PSM results, where the

TABLE 4 System GMM regressions of ownership structure on excess of executive total and cash compensation

Variable	EETC				EECC			
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
UK	−.180***	−.469***	−.191***	−.309***	−.369***	−.918***	−.546**	−.371***
	(−7.27)	(−19.32)	(−8.14)	(−4.28)	(−11.27)	(−11.04)	(−5.65)	(−8.73)
Ownership structure								
DIROWN	.001***			.007***	.001***			.001***
	(5.86)			(7.14)	(8.37)			(3.76)
INSOWN		.002***		.004***		.001***		.001** (2.70)
		(13.92)		(7.38)		(2.71)		
HERFIN			.434***	1.213***			.829** (5.53)	.444***
			(9.00)	(9.90)				(10.84)
Control variables								
SIZE	.141***	.158***	.153***	.264***	.134***	.246***	.192***	.135***
	(44.55)	(44.22)	(34.86)	(24.73)	(35.75)	(18.27)	(14.54)	(22.12)
ROA	.006***	.008***	.006***	.005** (4.18)	.009***	.011***	.005***	.011***
	(25.37)	(22.58)	(20.32)		(33.05)	(7.37)	(3.36)	(28.17)
AGE	.206***	.158***	.224***	.168***	.232***	.071***	.224***	.165***
	(13.61)	(12.19)	(21.61)	(5.53)	(20.96)	(2.79)	(6.75)	(11.72)
FL	−.125***	−.129***	−.235***	.006 (0.13)	−.167***	−.030	−.353***	−.051**
	(−5.55)	(−7.51)	(−11.22)		(−11.74)	(−0.49)	(−4.80)	(−2.53)
Q	.001***	.002***	.001***	−.001	−.001***	−.001	.009***	−.001
	(4.32)	(6.07)	(5.15)	(−0.87)	(−3.93)	(−0.79)	(4.28)	(−0.52)
GPD	.003* (1.92)	−.005***	−.001	−.012***	−.020***	−.014***	−.019**	−.019***
		(−5.18)	(−1.02)	(−4.50)	(−15.66)	(−4.23)	(−5.91)	(−10.79)
CONS	−3.787***	−3.507***	−3.599***	−3.885***	−3.466***	−2.161***	−3.161***	−2.592***
	(−26.05)	(−33.36)	(−26.66)	(−14.60)	(−37.30)	(−8.14)	(−9.40)	(−19.99)
Industry dummies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year dummies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Tests								
F	1646***	3086***	5244***	73.54***	2884***	38.41***	29.64***	4.91***
z_1	.000	.000	.000	.000	.000	.000	.000	.000
z_2	.000	.000	.000	.000	.000	.000	.000	.000
Sargan	.588	.423	.902	.409	.456	.632	.541	.306

Notes: T statistic in parentheses. F statistic (test of combined significance); $z1$ and $z2$ are two Wald tests of the joint significance of the reported coefficients and the joint significance of the time dummy variables, respectively (asymptotically distributed as $\lambda 2$ under the null hypothesis of no relationship, probability is shown); Sargan is a test of the over-identifying restrictions, asymptotically distributed as $\lambda 2$ under the null hypothesis of no correlation between the instruments and the error term, probability is shown.
***Significance at 1% level.
**Significance at 5% level.
*Significance at 10% level.

propensity score indicates the difference in excess executive compensation, both in total and in cash, between UK firms and their Spanish matching firms. We use three methods of calculation matching scores: the nearest neighbor, the radius matching, and the Kernel matching methods. As can be seen, in all cases, the negative and significant coefficient values indicate that UK firms align better the compensation of their executives, which imply less level of excess

compensation, both in total and in cash payments. These results give robustness to our findings and confirm our previous ones obtained in the GMM estimations.

Consequently, considering all the above results, we can partially confirm H1a and fully confirm H2a. Specifically, regarding ownership structure (H1a), our results show that high level of ownership concentration in the hands of directors contribute to excess executive

TABLE 5 System GMM regressions of board characteristics on excess of executive total and cash compensation

Variable	EETC				EECC			
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
UK	−.611*** (−8.15)	−.053** (−2.44)	−.367*** (−3.02)	−.086** (−2.37)	−.717*** (−7.32)	−.444*** (−4.22)	−.419** (−4.46)	−.395*** (−5.25)
Board characteristics								
PIND	−.006*** (−8.84)			−.005*** (−13.70)	−.006** (−6.98)			−.009*** (−11.88)
DUAL		.331*** (34.99)		.286*** (17.00)		.346*** (7.43)		.238*** (7.03)
LNDIR			.466*** (4.21)	.484*** (23.86)			.719*** (9.04)	.558*** (10.62)
Control variables								
SIZE	.551*** (18.78)	.108*** (49.69)	.165*** (6.31)	.150*** (22.90)	.202*** (12.07)	.142** (10.30)	.202*** (11.69)	.147*** (14.27)
ROA	.008*** (8.88)	.004* (17.14)	.018*** (7.40)	.004*** (13.12)	.006*** (4.41)	.008*** (5.39)	.008*** (5.41)	.006*** (4.69)
AGE	.244*** (8.99)	.211*** (19.56)	.083* (1.75)	.152*** (7.61)	.208*** (7.24)	.200*** (6.28)	.118*** (3.85)	.166*** (7.17)
FL	−.321*** (−6.44)	−.286*** (−15.95)	−.195* (−1.87)	−.060** (−2.23)	−.314*** (−3.89)	−.502*** (−6.58)	−.114 (−1.34)	−.306*** (−4.26)
Q	.007*** (−6.44)	.001*** (4.66)	.005* (1.94)	.002*** (9.59)	.005** (2.25)	.001 (.70)	.002 (.66)	.003** (2.27)
GPD	−.009*** (−3.68)	−.000 (−0.05)	.008* (1.76)	.001 (1.47)	−.016*** (−4.48)	−.014*** (−4.19)	−.007* (−1.94)	−.018*** (−7.71)
CONS	−4.166*** (−16.40)	−3.318*** (−27.60)	−3.873*** (−7.86)	−4.096*** (−19.68)	2.852** (−10.33)	2.910*** (−8.48)	−3.892*** (−9.98)	−3.698*** (−13.93)
Industry dummies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year dummies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Tests								
F	62.12***	2828***	21.35***	28834***	25.04***	44.97***	25.27***	73.49***
z_1	.000	.000	.000	.000	.000	.000	.000	.000
z_2	.000	.000	.000	.000	.000	.000	.000	.000
Sargan	.305	.407	.428	1.000	25.04	.518	.554	.558

Notes: T statistic in parentheses. F statistic (test of combined significance); z_1 and z_2 are two Wald tests of the joint significance of the reported coefficients and the joint significance of the time dummy variables, respectively (asymptotically distributed as $\lambda 2$ under the null hypothesis of no relationship, probability is shown); Sargan is a test of the over-identifying restrictions, asymptotically distributed as $\lambda 2$ under the null hypothesis of no correlation between the instruments and the error term, probability is shown.
***Significance at 1% level.
**Significance at 5% level.
*Significance at 10% level.

compensation and that, contrary to our expectations, the presence of institutional owners do not does not avoid agency costs associated with misalignment of executive compensation. Concerning board characteristics (H2a), we find that small board dominated by independent directors and with non-dual structures positively influence the executive compensation alignment, reducing excess compensation. On the other hand, when we analyzed the moderating effects by country our findings confirm the governance context effect and,

therefore, the influence of institutional environment in the context of corporate governance formulated in H1b and H2b. Specifically, we confirm H1b since we find that ownership concentration, institutional and directors ownership exert a more effective monitoring over executive compensation in the United Kingdom than in Spain. Regarding boards, we confirm H2b since independent directors, duality, and (less) board size are more related with the effectiveness in executive compensation in the United Kingdom than in Spain.

TABLE 6 System GMM regressions of the relationship between ownership structure and excess of executive total and cash compensation including moderating effects

	EETC			EECC		
Variable	Model I	Model II	Model III	Model I	Model II	Model III
UK	−.272*** (−5.46)	−.146*** (−4.30)	−.361*** (−6.68)	−.402*** (−10.58)	−.327*** (−7.72)	−.561*** (−11.75)
Moderating effects						
UK * DIROWN	−.005*** (−7.75)			−.005*** (−10.74)		
UK * INSOWN		−.003** (−9.87)			−.004*** (−11.10)	
UK * HERFIN			−13.976*** (−8.00)			−13.542*** (−9.47)
Ownership structure						
DIROWN	.002*** (4.53)	.001*** (3.19)	.004*** (7.02)	.002*** (5.96)	.001* (1.69)	.003*** (7.05)
INSOWN	.003*** (14.34)	.004*** (26.07)	.003*** (12.26)	.001*** (4.88)	.002*** (12.24)	.002*** (6.55)
HERFIN	.798*** (12.77)	.482*** (10.72)	.530*** (4.75)	.788*** (15.32)	.388*** (11.65)	.688*** (6.60)
Control variables						
SIZE	.201*** (3.02)	.150*** (26.62)	.229*** (24.96)	.180*** (30.36)	.134*** (30.47)	.222*** (29.99)
ROA	.009*** (24.78)	.008*** (16.68)	.011*** (10.03)	.011*** (28.86)	.012*** (31.77)	.017*** (18.90)
AGE	.156*** (7.43)	.144*** (12.54)	.138*** (6.19)	.143*** (7.24)	.149*** (14.09)	.142*** (7.31)
FL	.107*** (5.38)	−.029* (−1.77)	−.048 (−1.15)	.007 (0.33)	−.083*** (−4.12)	−0.010 (−0.27)
Q	.004*** (13.93)	.003*** (4.44)	−.002** (−2.08)	.002*** (7.44)	−.001 (−0.71)	−.006*** (−4.77)
GPD	−.005*** (−4.59)	.001 (0.50)	−.013*** (−5.06)	−.021*** (−11.70)	−0.017*** (−13.57)	−.026*** (−8.42)
CONS	−3.495*** (−15.34)	−2.777*** (−23.29)	−3.521*** (−15.88)	−2.904*** (−13.58)	−2.363*** (−20.79)	−3.079*** (−17.36)
Industry dummies	Yes	Yes	Yes	Yes	Yes	Yes
Year dummies	Yes	Yes	Yes	Yes	Yes	Yes
Tests						
F	450.56***	3569***	270.75***	932.72***	4060.61***	548.35***
z_1	.000	.000	.000	.000	.000	.000
z_2	.000	.000	.000	.000	.000	.000
Sargan	1.000	0.396	777.82	1.000	0.368	0.210

Notes: T statistic in parentheses. *F* statistic (test of combined significance); *z*1 and *z*2 are two Wald tests of the joint significance of the reported coefficients and the joint significance of the time dummy variables, respectively (asymptotically distributed as λ2 under the null hypothesis of no relationship, probability is shown); Sargan is a test of the over-identifying restrictions, asymptotically distributed as λ2 under the null hypothesis of no correlation between the instruments and the error term, probability is shown.
***Significance at 1% level.
**Significance at 5% level.
*Significance at 10% level.

5 | CONCLUSIONS

5.1 | Main findings and academic contributions

The influence of governance mechanisms on executive compensation has been the subject of extensive study (Devers et al., 2007; Murphy, 2013). However, the examination of the contextual effects of governance has mostly been neglected. As La Porta and colleagues report (Johnson et al., 2000; La Porta et al., 1999), the mechanisms of corporate governance are not equally effective in all countries. The institutional context determines, to a marked extent, the effectiveness of these mechanisms, with the monitoring of executive compensation being a prime example (Aguilera et al., 2008; Baixauli-Soler & Sánchez-Marín, 2011).

This paper thus contributes to this stream of research focusing on how the national–institutional contexts of corporate governance determines the effectiveness of a firm's governance mechanisms (Judge et al., 2008), with specific consequences in terms the alignment

TABLE 7 System GMM regressions of the relationship between board characteristics and excess of executive total and cash compensation including moderating effects

Variable	EETC			EECC		
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
UK	−.164*** (−3.48)	−.054* (−1.93)	−1.321*** (−4.22)	−.161*** (−4.13)	−.283*** (−5.73)	−1.412*** (−4.72)
Moderating effects						
UK * PIND	−.003** (−3.53)			−.004*** (−6.71)		
UK * DUAL		−.249*** (−8.39)			−.195** (−2.46)	
UK * LNDIR			.388** (3.11)			.303* (2.44)
Board characteristics						
PIND	−.009*** (−12.11)	−.009*** (−23.43)	−.004*** (−2.76)	−.002** (−3.74)	−.004*** (−14.52)	−.003*** (−3.16)
DUAL	.132*** (5.65)	.452*** (26.45)	.113** (2.28)	.276*** (16.26)	.361*** (9.83)	.095* (1.91)
LNDIR	.899*** (24.41)	.647*** (27.37)	.042 (0.40)	.530*** (24.72)	.534*** (21.07)	.156 (1.56)
Control variables						
SIZE	.170*** (18.15)	.175*** (44.11)	.215*** (9.34)	.136*** (26.16)	.137*** (27.29)	.190*** (9.88)
ROA	.009*** (9.26)	.007*** (14.08)	.008*** (2.85)	.007*** (22.81)	.007*** (23.49)	.009*** (3.61)
AGE	.127*** (6.71)	.163*** (13.67)	.149*** (3.47)	.151*** (7.31)	.136*** (7.91)	.083** (2.21)
FL	−.193*** (−3.87)	−.157*** (−5.93)	−.253* (−1.92)	−.118*** (−4.91)	−.166*** (−6.55)	−.393*** (−3.45)
Q	.001 (−0.63)	.007*** (16.37)	.004 (1.54)	.001 (0.29)	.001** (2.14)	.008*** (3.12)
GPD	.001 (0.55)	−.001 (−0.14)	.002 (0.61)	−.014*** (−7.22)	−.019*** (−11.89)	−.005 (−1.06)
CONS	−4.655*** (−27.25)	−4.445*** (−39.90)	−2.849*** (−6.26)	−3.580*** (−18.47)	−3.785*** (−21.14)	−1.976** (−5.01)
Industry dummies	Yes	Yes	Yes	Yes	Yes	Yes
Year dummies	Yes	Yes	Yes	Yes	Yes	Yes
Tests						
F	306.32***	72089***	14.13***	2993.95***	940.56***	19.13***
z_1	.000	.000	.0000	.000	.000	.000
z_2	.000	.000	.000	.000	.000	.000
Sargan	.657	.488	.492	.998	1.000	.923

Notes: T statistic in parentheses. F statistic (test of combined significance); $z1$ and $z2$ are two Wald tests of the joint significance of the reported coefficients and the joint significance of the time dummy variables, respectively (asymptotically distributed as $\lambda2$ under the null hypothesis of no relationship, probability is shown); Sargan is a test of the over-identifying restrictions, asymptotically distributed as $\lambda2$ under the null hypothesis of no correlation between the instruments and the error term, probability is shown.

***Significance at 1% level.
**Significance at 5% level.
*Significance at 10% level.

of executive compensation (Core et al., 2008; Sapp, 2008). Basing on the empirical evidence provided on a sample of UK and Spanish listed firms during the period 2005–2012, our findings also provide new insights into more specific areas in corporate governance and executive compensation literature. First, in line with the emerging literature based on comparative systems of corporate governance (Cucari, 2019; Paniagua et al., 2018), this paper voids the gap regarding the lack of specific pair comparison—in depth and in detail—about how executive compensation is determined by the two main models of corporate governance using two of the most representative countries in Europe of these models. Second, through the concept of "excess compensation," this research helps to identify theoretically

and empirically—based on subsequent developments of the model of Core et al. (1999, 2008)—how the degree of efficiency of the governance mechanisms impacts on the pay-for-performance alignment (Brunarski et al., 2015). And third, institutional arguments that complements agency considerations in explaining the links between corporate governance and executive compensation allow this research to show a fuller and enriched picture of these relationships (Baixauli-Soler & Sánchez-Marín, 2015).

Our findings are grounded on the idea that a firm's insiders and outsiders will have different incentives, abilities, and rights depending on the institutional context in which they operate, and that national contextual circumstances influence the effectiveness of the

TABLE 8 Propensity score matching United Kingdom versus Spain on excess of executive total and cash compensation

	Nearest neighbor method	Radius matching method	Kernel matching method
EETC (UK)	−1.056*** (0.271)	−.651*** (0.139)	−.785*** (0.175)
EECC (UK)	−1.336*** (0.274)	−.9212*** (0.139)	−1.065*** (0.176)
Matching variables			
SIZE	Yes	Yes	Yes
ROA	Yes	Yes	Yes
AGE	Yes	Yes	Yes
FL	Yes	Yes	Yes
Q	Yes	Yes	Yes
GPD	Yes	Yes	Yes
Industry dummies	Yes	Yes	Yes
Year dummies	Yes	Yes	Yes

Note: SD in parentheses.
***Significance at 1%.

governance mechanisms used by firms (Young et al., 2008). The characteristics of the respective UK and Spanish systems of corporate governance (common law vs. civil law, minority shareholders' legal protection, and capital market development) lead to alternative types of agency conflict—between executives and shareholders in the United Kingdom and between majority and minority shareholders in Spain—that significantly influence the effectiveness of the ownership structure and of the board of directors as the two main mechanisms of monitoring executive compensation (Conyon et al., 2011). The UK firms' more favorable institutional context and more effective governance mechanisms lead to a more efficient alignment of executive compensation whereas Spanish firms shows more excess executive compensation that implies the assumption of more agency cost as a consequence of less effective monitoring mechanisms.

Although our results generally confirm—in line with our expectations—the above evidence, a more detailed, fine-tuned, analysis of findings give light to a more deeply knowledge of governance mechanisms' influences in executive compensation. The moderating effects by country confirm the institutional governance context effect: ownership concentration, institutional and directors' ownership exert a more effective monitoring over executive compensation in the United Kingdom than in Spain. Regarding boards, independent directors, duality, and smaller board size are more related with the effectiveness in executive compensation in the United Kingdom than in Spain. In this vein, it is interesting to consider that although the presence of institutional owners by their selves do not avoid agency costs associated with misalignment of executive compensation, when we consider the country effect of governance, institutional investors significantly differentiate their influence, more aligned in the case of UK firms than in Spanish companies.

Finally, and considering other contexts of corporate governance like those of emerging economies, we can conclude a certain similarity with that of Spain. As Young et al. (2008, p. 196) state, "in emerging economies, the institutional context makes the enforcement of agency contracts more costly and problematic" resulting in the prevalence of concentrated firm ownership in the hands of majority, board-dominant shareholders which, combined with an absence of effective external governance mechanisms, results in more frequent principal–principal conflicts (Morck et al., 2005). Notwithstanding this similarity, due to the wide internationalization of companies and the need to follow international management standards, external and institutional pressures for good governance facing Spanish listed firms are higher (Aguilera et al., 2008; Baixauli-Soler & Sánchez-Marín, 2015). Since owners and boards are required to implement more rational, aligned governance mechanisms, and considering executive compensation as one of the most prominent and legitimacy signaling practice of good governance (Judge et al., 2008), Spanish executives show moderate levels—higher than the United Kingdom but lower than in firms of emerging economies—of excess compensation.

5.2 | Practical implications

In terms of practical implications, this study suggests that differences in the UK–Spain executive pay efficiency arise because of differences in corporate governance characteristics that have their roots in legal origins, institutional arrangements, and country culture between the two economies. Understanding the degree of similarity, differences, and convergence in corporate governance regimes is, of course, complex (Conyon & He, 2011), but this research is a first step in the knowledge of this topics and their influence in executive compensation.

Our study's findings suggest that to improve the efficiency—and reducing the excess—of executive compensation in countries with Continental European system such as Spain, institutions, and firms must (Sánchez-Marín et al., 2017; Sánchez-Marín & Baixauli-Soler, 2014): (1) encourage market discipline to promote better functioning of external governance mechanisms (e.g., through the market for corporate control); (2) take action to strengthen the property

rights of minority shareholders and to tackle statutory covenants that limit voting rights; and (3) foster greater transparency and disclosure in corporate governance reports, especially in relation to the compensation policies, thereby facilitating the creation of trust and legitimacy and discouraging inappropriate and possibly selfish behavior.

Regulatory and legislative initiatives have a vital role to play in addition to—and complementary with—the existing *Código de Buen Gobierno de las Sociedades Cotizadas* (Comisión Nacional del Mercado de Valores, 2020) (Code of Good Governance of Listed Companies), based on similar principles to those of the Cadbury Code (1992). It remains to be seen whether such initiatives are enough to create the appropriate mechanisms for monitoring executive compensation and generating social reputation and legitimacy, while not limiting the necessary managerial discretion of firms.

In addition, public institutions should encourage the implementation of new corporate governance mechanisms in listed companies that give voice to minority shareholders and promote the so-called "shareholders activism" (Lozano-Reina & Sánchez-Marín, 2020; Stathopoulos & Voulgaris, 2016). Mechanisms such as "say-on-pay" allows shareholders, through a voting on which shareholders express their agreement or disagreement with executives' pay policies, have the opportunity to have a positive influence on the alignment and optimization of executive compensation (Baixauli-Soler et al., 2021; Correa & Lel, 2016). Although generally advisory and non-binding, this mechanism has a potential impact on executive compensation, as its results can be interpreted as "motions of confidence" or "wake-up calls" to the top executive team regarding the management of the company (Lozano-Reina et al., 2021).

5.3 | Limitations and lines of future research

Finally, this research is not without limitations, which can be considered for new and future research in this line of investigation. First, although our study analyzes in detail the influence of governance mechanisms on the executive compensation alignment in two representative countries of the two dominant corporate governance systems (the United Kingdom and the Anglo-Saxon system vs. Spain and the Continental European system), our findings cannot necessarily be extrapolated or generalized to the rest of the countries under one or the other system, due to the governance idiosyncrasies of each specific country (Aguilera et al., 2008; Aguilera & Desender, 2012). Further research is therefore needed with a broader sample spectrum that extend analyses to other key countries in these governance systems—such as the United States for the Anglo-Saxon or Germany or France for the Continental European—in order to know more precisely how the characteristics and effectiveness of their corporate governance mechanisms influence the alignment of executive compensation. Second, our data available of both countries are limited to the period 2005–2012. Although these 8 years panel data offer consistent and stable information about corporate governance characteristics that potentially influence executive compensation, future studies should update information in order to check results

consistency in the face of more current data. Third, even though our results shed light on the executive compensation and governance mechanisms relationships in the United Kingdom and Spain, this research lack of more detailed information regarding the compensation of all types of executives (CEOs, executive directors, and executive non-directors) who belong to the top management team. New studies should analyze specific relationships between the executive compensation, executive position, and corporate governance in order to obtain a more whole picture of these relationships. Fourth, future research should explore in deep how the specific nature and motivations of majority shareholders—family versus non-family; individuals versus firms; institutional versus non-institutional—influence effectiveness of monitoring and excess executive compensation. Finally, although this research emphasizes the role of institutional context in the effectiveness of governance mechanisms, future studies should complete the picture by explicitly considering the role of external mechanisms of governance (capital and labor markets, indicators of legal regulations, etc.) and their effects in executive compensation.

DATA AVAILABILTY STATEMENT

The data that support the findings of this study are openly available in Zenodo online (https://doi.org/10.5281/zenodo.5794495), following an embargo to allow for publication of research findings.

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ENDNOTE

[1] Direct shares are shares of the focal company. Indirect shares are shares of the focal company by virtue of owing shares of another company.

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