

# PYRAMIDAL STRUCTURES IN POLAND

## Introduction

Ownership structure remains the crucial company's characteristics, it belongs to the most important governance mechanisms, and delivers fundamental legacy for oversight and control. The studies on ownership structure patterns, dynamics and characteristics help understand the directions of strategic development of companies. The growing interest in the comparative analysis delivers insights into the studies of different ownership types and form, shareholder identities and the logic of their operation. Interestingly, the literature dominated by the research on the dispersed ownership and Anglo-Saxon economies placed the ownership structure studies in the framework of principal agent theory and conflicts between executives and shareholders. Moreover, the largest companies in other countries also depict such ownership pattern and face – in the language of agency theory – the problems of hidden action, hidden information and hidden intention. Further comparative research indicated the concentrated ownership as the dominant pattern for control. The concentrated ownership is revealed in continental Europe, Latin America, Australia, Asia (Morck, 2002; Morck, 2009). Moreover, in many companies the concentrated ownership is not only the result of the simple majority stake held by the dominant shareholder but is tied to the control exerted via pyramidal structures which allow to lower the capital involvement. The pyramidal structures depicted in line of the comparative analysis of emerging markets are revealed in India, South Korea, Thailand, Russia, Ukraine, Latin American countries (mostly researched – Mexico, Brazil, Chile, Peru, Argentina). Interestingly, pyramidal structures are also to be found in developed economies such as Canada, Belgium, Italy, France, Sweden (Aluchna, 2010). Despite the extensive evidence on some negative motivations for creating pyramidal structures such as tunneling and abuse of minority shareholders, there is a growing number of

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\* **Maria Aluchna, Ph.D.** – Department of Management Theory, Warsaw School of Economics.

studies suggesting that pyramids do not destroy shareholder value but simply serve as a tool for control exerted over the companies by their founders.

The paper presents the essential dimensions of ownership structure focusing on its specific form known as pyramids. The aim of the paper is to analyze the reasons for creating and logic of functioning of pyramidal structures and to deliver a brief presentation of the pyramidal structures identified in Poland amongst the largest public listed companies. The paper is organized as follows. The first section provides a literature review presenting the theme of pyramidal structures as the specific form of ownership and control pointing out at the reasons behind their creation and the logic of their functioning. The characteristics of the ownership structure of Polish companies with the discussion of its strengths and challenges is outlined in the second section. The third section delivers the initial results on the analysis of the pyramidal structures identified amongst the largest public companies listed on the Warsaw Stock Exchange. The final remarks are presented in the conclusion section.

## 1. Ownership structure

The analyses on ownership structure usually distinguish its two types: dispersed ownership and concentrated ownership. Additionally, for the purpose of studies the identity of shareholders is analyzed identifying individual and institutional shareholders, state ownership, managerial ownership as well as the presence of financial and non financial institutions in the ownership structure. The analysis of ownership structure allows to relate a specific ownership patterns and characteristics to company behavior, strategy and performance. For instance dispersed ownership offers a lot of opportunities for raising significant funds and risk diversification, it leads, however, to increased principal-agent conflicts as the residual rights of control are in the hands of executives (Monks and Minow, 2004). Shareholders face the limited possibility to monitor and control executives and experience the problems of hidden action, hidden information and hidden intention (Jensen and Meckling, 1976; Shleifer and Vishny, 1997). Dispersed ownership also is characterized with the free rider problem as the holders of small stakes are not interested in collecting and processing information for the evaluation of the executives. They remain passive and vote by feet, not getting involved in the supervision and governance (Monks and Minow, 2004). The concentrated ownership is seen as the solution to agency conflicts and free rider problem (Jensen and Meckling, 1976; Shleifer and Vishny, 1997) and is believed to lead to higher profitability when the dominating owners are active (Neun and Santerre, 1986; Holderness and Sheehan, 1988). The ownership concentration proves to be an important monitoring mechanism being the second best solution

when market/ external mechanisms are not working well (Morck and Steier, 2005). The majority shareholder is able to internalize the costs of collecting information and to exert effective control over management as they possess significant stakes and crucial know-how. The active engagement in monitoring and control appears to be an efficient strategy for majority shareholders. Some doubts refer however to the threat of the majority shareholder abusing their position via representatives on the board favoring them at the cost of minority shareholders (Fama and Jensen, 1983). The dominant shareholders may expropriate minority shareholders through a tunneling or compensation policy (Stulz, 1988), blocking dividend payout or limiting access to information.

With the reference to shareholder identity most studies focus on the effects of institutional and managerial ownership. The involvement of institutional investors in the ownership structure is positively correlated with corporate performance due to their skills and experience in monitoring (Brickley et al., 1988; McConnell and Servaes, 1990; Useem, 1996; Maug, 1998; Woitke, 2002; Faccio and Lasfer, 2000). Managerial ownership is also believed to increase executives' motivation for creating shareholder value and to improve corporate performance. Research indicates that the positive effects are noted when the manager owns a stake between 0–5% and above 25% of shares (Morck et al., 1988).

The comparative analysis reveals that the dispersed ownership is mostly found in Anglo-Saxon economies and in the case of the largest companies worldwide. Continental European countries are characterized by significant ownership concentration (Allen and Gale, 2000; Murphy, 2003; Frohlin, 2003; Aganin and Volpin, 2003; Högfeldt, 2003) which results in the limited number of shareholders and the dominance by powerful owner over the company. A similar pattern is also depicted in companies in Latin America and Asia (Morck et al., 2004). The ownership concentration is connected to a different specificity of shareholder identity – families and non financial institutions play an important role in the ownership structure for continental Europe, Latin America and Asia. Table 1 presents ownership structure in selected countries with reference to the degree of ownership concentration and family control.

As shown in Table 1 dispersed ownership is reported mostly in Anglo-Saxon countries. Concentrated ownership and control by families is found mostly in continental Europe and Asia.

Table 1. Ownership structure in selected countries

Country	10% threshold		20% threshold		Source
	Dispersed ownership	Family control	Dispersed ownership	Family control	
Argentina	0	65	0	65	La Porta et al. (1999, table 2 and 3)
Australia	55	10	65	5	La Porta et al. (1999, table 2 and 3)
Austria	5	15	5	15	La Porta et al. (1999, table 2 and 3)
Belgium	0	50	5	50	La Porta et al. (1999, table 2 and 3)
Canada	50 17.54	30 46.67	60 36.24	25 26.18	La Porta et al. (1999, table 2 and 3) Attandg, Gradhoum, Lang (2003)
Denmark	10	35	40	35	La Porta et al. (1999, table 2 and 3)
Finland	15	10	35	10	La Porta et al. (1999, table 2 and 3)
France	30 8.92	20 70.44	60 17.79	20 64.83	La Porta et al. (1999, table 2 and 3) Faccio, Lang (2002)
Germany	35	10 74.64	50 14.02	10 64.62	La Porta et al. (1999, table 2 and 3) Faccio, Lang (2002)
Greece	5	65	10	50	La Porta et al. (1999, table 2 and 3)
Hong Kong	10 0.6	70 64.7	10 7	70 66.7	La Porta et al. (1999, table 2 and 3) Claessens, Djankov, Lang (2000)
Indonesia	0.6	68.6	5.5	71.5	Claessens, Djankov, Lang (2000)
Ireland	45	15	65	10	La Porta et al. (1999, table 2 and 3)
Israel	5	50	5	50	La Porta et al. (1999, table 2 and 3)
Italy	15 7.83	20 64.87	20 15.86	15 59.61	La Porta et al. (1999, table 2 and 3) Faccio, Lang (2002)
Japan	50 42	10 13.1	90 79.8	5 9.7	La Porta et al. (1999, table 2 and 3) Claessens, Djankov, Lang (2000)
Korea	40 14.3	35 67.9	55 43.2	20 48.4	La Porta et al. (1999, table 2 and 3) Claessens, Djankov, Lang (2000)
Malaysia	1	57.5	10.3	67.2	Claessens, Djankov, Lang (2000)
Mexico	0	100	0	100	La Porta et al. (1999, table 2 and 3)
Holland	30	20	30	20	La Porta et al. (1999, table 2 and 3)
New Zealand	5	45	30	25	La Porta et al. (1999, table 2 and 3)
Norway	5	25	25	25	La Porta et al. (1999, table 2 and 3)
Philippines	1.7	42.1	19.2	44.6	Claessens, Djankov, Lang (2000)
Portugal	5	50	10	45	La Porta et al. (1999, table 2 and 3)
Singapore	5 1.4	45 52	15 5.4	30 55.4	La Porta et al. (1999, table 2 and 3) Claessens, Djankov, Lang (2000)
Spain	15 12.74	25 67.33	35 28.06	15 55.79	La Porta et al. (1999, table 2 and 3) Faccio, Lang (2002)
Sweden	0	55	25	45	La Porta et al. (1999, table 2 and 3)
Switzerland	50	40	60	30	La Porta et al. (1999, table 2 and 3)
Taiwan	2.9	65.6	26.2	48.2	Claessens, Djankov, Lang (2000)

Thailand	2.2	56.5	6.6	61.6	Claessens, Djankov, Lang (2000)
UK	90 27.06	5 33.75	100 69.08	0 19.88	La Porta et al. (1999, table 2 and 3) Faccio, Lang (2002)
US	80 38.95	20 23.37	80 69.26	20 6.13	La Porta et al. (1999, table 2 and 3) Attig, Gradhoum, Lang (2003)

Source: Morck R., Wolfenzon D., Yeung B. (2004), *Corporate governance, economic entrenchment and growth*, NBER Working Paper No. 10692, p. 8.

## 2. Pyramids as a specific form of ownership structure

The ownership concentration, involvement of families or financial and industrial companies as well as the preferred shares which companies are allowed to use have very often related to the popularity of pyramidal structures (Morck et al., 2004; Bebchuck, 1999). Pyramidal structures are the ownership type constituting of multi level companies with cross shareholdings which form relations of control (Zattoni, 1998; Bennedsen and Nielsen, 2006). The dominant shareholder via the controlling (holding) company exerts control and influence on decision making and profit distribution over all the portfolio companies, many of which may be listed (Cuervo-Cazzura, 2006). The main listed company is located at the apex of the pyramid and is controlled via the chain of subsidiaries, many of which do not report any operational activity but serve as financial and holding vehicles. Pyramidal structures do not replace preferred shares (they are more popular), although sometimes companies adopt both techniques of separating control and cash flow rights (Almeida and Wolfenzon, 2005). The characteristics of pyramidal structures, preferred shares and multi-level connections between different shareholders limit the transparency of continental European companies and are heavily criticized by Anglo-Saxon and pro-investor representatives. Pyramidal structures are often reported in economies of Germany, France, Sweden as well as Italy. Pyramids are also the popular ownership form in Latin America, Asia, Canada and Central and Eastern Europe. They very rarely are found in Anglo-Saxon countries. Table 2 presents mechanisms of separation control and cash flow rights in Europe addressing the aspects of the use of preferred shares, pyramids and cross shareholdings.

As shown in Table 2 pyramids are revealed in many European countries, mostly in Italy, France, Belgium, Austria, Germany, Norway and Sweden. Also the use of preferred shares is reported across European economies.

The separation of control and cash flow rights via the adoption of preferred shares and building multilayer pyramidal structures allow the dominant shareholder (founder, family) to exert full control over the group and assure for control at the lower capital involvement of the majority shareholder. Although separation of control and cash flow

rights motivates controlling shareholders to list publicly the company from the group and improves risk diversification, it may also lead to abuse of minority shareholders (investment policy and dividend payouts) and tunneling (Zattoni, 1999). Thus, the problems of pyramids corresponds to the classical negative consequences of concentrated ownership characterized by the majority owners abusing minority shareholders.

Table 2. Mechanisms of separation control and cash flow rights in Europe

Country	Sample	Preferred shares		Pyramids		Cross shareholdings		Other		Total	
		No. of firms	% firms	No. of firms	% firms	No. of firms	% firms	No. of firms	% firms	No. of firms	% firms
Austria	90	21	0.23	23	0.26	1	0.01	0	0.00	39	0.43
Belgium	85	0	0.00	23	0.27	0	0.00	5	0.06	28	0.33
Denmark	164	48	0.29	28	0.17	0	0.00	9	0.05	75	0.46
Finland	104	46	0.44	7	0.07	0	0.00	7	0.07	56	0.54
France	495	15	0.03	72	0.15	0	0.00	0	0.00	86	0.17
Germany	582	112	0.19	137	0.24	18	0.03	3	0.01	233	0.40
Ireland	60	15	0.43	11	0.18	0	0.00	2	0.03	25	0.42
Italy	169	73	0.43	42	0.25	2	0.01	1	0.01	93	0.55
Norway	138	15	0.11	45	0.33	3	0.02	1	0.01	57	0.41
Portugal	70	0	0.00	9	0.13	0	0.00	0	0.00	9	0.13
Spain	146	0	0.00	24	0.16	0	0.00	3	0.02	27	0.18
Sweden	200	123	0.62	53	0.27	1	0.01	0	0.00	147	0.74
Switzerland	161	84	0.52	10	0.06	0	0.00	0	0.00	93	0.58
UK	1632	411	0.25	358	0.22	2	0.00	10	0.01	689	0.42
Total	4096	963	0.24	842	0.21	27	0.01	41	0.01	1657	0.40

Source: Bennedsen M., Nielsen K. (2006), *The principle of proportional ownership, investors protection and firm value in Western Europe*, ECGI working paper No. 134, p. 37.

### 3. Pyramids in Poland

Polish listed companies reveal significant concentration of ownership characterized by the average majority shareholder stake estimated at 41% shares (Kozarzewski, 2003; Dzierzanowski and Tamowicz, 2002; Aluchna, 2007; Urbanek, 2009). The most popular types of dominant shareholders include domestic and foreign strategic investors and private investors (entrepreneurs who serve as CEOs). Although financial investors contribute to the number of shareholders, they prefer to hold smaller stakes and remain relatively passive in monitoring and governance (Kozarzewski, 2006; Dzierzanowski and Tamowicz, 2002).

The ownership structure analysis depicts a slight evolution of the identity of the dominant shareholder and the degree of ownership concentration resulting mostly from the economic development and the expansion of domestic companies. The early analyses pointed out the strategic foreign investors as the dominant group of shareholders which are now taken over by domestic shareholders. The domestic private and domestic strategic investors become the most frequent identity of dominant shareholder of Polish listed companies as presented in Table 3.

Table 3. Ownership structure of Polish companies (No. of sample companies, % of sample companies)

Shareholder category	1 <sup>st</sup> largest	2 <sup>nd</sup> largest	3 <sup>rd</sup> largest	4 <sup>th</sup> largest
Top Management Team members	88 (25.1%)	49 (17.3%)	31 (15.3%)	18 (14.5%)
Supervisory board directors	39 (11.4%)	40 (14.1%)	28 (13.8%)	12 (9.7%)
Other individual	24 (7.1%)	24 (8.5%)	25 (12.3%)	13 (10.5%)
Strategic foreign investor	60 (17.1%)	18 (6.4%)	8 (3.9%)	5 (4.0%)
Financial foreign investor	6 (1.7%)	14 (4.9%)	9 (4.4%)	5 (4.0%)
Strategic domestic investor	71 (20.3%)	26 (9.2%)	16 (7.9%)	6 (4.8%)
Financial domestic investor	28 (8.0%)	66 (23.3%)	47 (23.2%)	42 (33.9%)
NIF	4 (1.1%)	2 (0.7%)	–	–
Pension fund	7 (2.0%)	36 (12.7%)	35 (17.2%)	20 (16.1%)
State	14 (4.0%)	4 (1.4%)	1 (0.5%)	1 (0.8%)
Cross shareholding (to be liquidated)	4 (1.1%)	4 (1.4%)	3 (1.5%)	2 (1.6%)
Dispersed ownership	7 (2.0%)	–	–	–
Total	350 (100%)	283 (100%)	203 (100%)	124 (100%)

Source: compilation based on Urbanek (2009), pp. 392–393.

Table 3 reveals a significant popularity of domestic individual investors as the majority shareholders of Polish listed companies who aim at keeping the controlling share despite their companies IPOs. Although not shown in Table 3, the trend of creating corporate groups controlled by the domestic investors (individual or family) appears to be a strong phenomenon noted recently (Aluchna, 2010).

In order to provide some insights in the trends of the ownership structure and the popularity of pyramids among the listed companies, an additional analysis has been conducted. Table 4 presents the characteristics of 30 largest companies listed at the Warsaw Stock Exchange (as of the end of 2011) with respect of the degree of ownership concentration (concentrated or dispersed), the dominant shareholder (stake and name of the company, institution or individual investor), the use of the pyramidal structure and the adoption of preferred shares.

Table 4. Ownership structure of 30 largest public listed companies

Company	Ownership structure	Dominant shareholder	Pyramidal structure	Preferred shares
PGE	Concentrated	State – 85%	No	No
PGNiG	Concentrated	State – 73.5%	No	No
TP SA	Concentrated	France Telecom – 49.7%	No	No
KGHM	Concentrated	State – 42%	No	No
PKN Orlen	Concentrated	State – 27%	No	No
Enea	Concentrated	State – 60.4%	No	No
GTC	Concentrated	GTC Real Estate Holding B.V. – 46%	Yes – 2 levels	No
Żywiec	Concentrated	Brau Union AG – 62%	Yes – 4 levels	No
TVN	Concentrated	ITI – 64%	Yes – at least 2 levels	No
Asseco Poland	Dispersed	Asseco Poland – 12% A. Góral – 11%	No	No
Cyfrowy Polsat	Concentrated	Polaris Finance BV – 68.2% C, 78.53% V	Yes – at least 2 levels	Yes
Świecie	Concentrated	Framondi NV – 66%	Yes – at least 2 levels	No
Lotos	Concentrated	State – 53.2%	No	No
Stalprodukt	Concentrated	Arcelor Mittal – 38%	Yes – at least 2 levels	Yes
LPP	Concentrated	M. Piechocki – 33%, J. Lubianiec 29%	No	Yes
PBG	Concentrated	J. Wiśniewski – 45.7%	No	Yes
Bogdanka	Concentrated	State – 60.5%	No	No
Eurocash	Concentrated	L. Amaral plus subsidiary Politra B. V – 53%	Yes – at least 2 levels	No
NG2	Concentrated	D. Miłek i Luxprofi – 50.5%	Yes – at least 2 levels	Yes
Cersanit	Concentrated	M. Sołowiow (directly and indirectly) – 48.6%	Yes – at least 2 levels	No
Polimex Mostostal	Dispersed	ING – 8.7%	No	No
Budimex	Concentrated	Ferrovial 59%	Yes – at least 2 levels	No
Kopex	Concentrated	K. Jędrzejewski – 60.4%	Yes – at least 2 levels	No
Netia	Rather dispersed	Third Avenue Management LLC 24%	No	No
Orbis	Concentrated	Accor – 50.01%	Yes – at least 2 levels	No
Echo	Concentrated	M. Sołowiow (directly and indirectly) – 4%	Yes – at least 2 levels	No
Emperia	Dispersed	Aviva CU – 9.8%	No	No
InterCars	Concentrated	K. Oleksowicz – 35%	No	No
MMPL	Concentrated	3 holding subsidiaries – 56%	Yes, at least 2 levels	No
AMREST	Dispersed	BZ WBK Asset Management SA 22%	No	No

Source: own compilation based on the annual reports of the analyzed companies.



As shown in Table 4.25 out of 30 sample companies reveal concentrated ownership, which is consistent with previous studies (Kozarzewski, 2003; Dzierzanowski and Tamowicz, 2002; Aluchna, 2007; Urbanek, 2009). It is important to emphasize that ownership concentration is depicted also amongst the largest companies which usually tend to show a lesser degree of ownership concentration. The analysis also indicates that 14 out of 30 analyzed companies adopt pyramidal structure in their ownership. The pyramids are usually formed in the case of companies which were privatized to the strategic investors and which were founded after 1990 by individual investors. Pyramids are usually formed in the case of corporate groups with the listed company controlled by the strategic investor (Aluchna, 2010). Interestingly, the state control in the ownership structure translates into absence of pyramidal structure patterns in Polish companies. Additionally, 4 out of 30 analyzed companies use preferred share, which means that 16 of the sample firms adopt mechanisms of separation of control and cash flow rights. This initial analysis does not allow for any conclusion on the reasons behind the adoption of the pyramidal structures by Polish listed companies. In line however with previous research the most likely reasons refer to the aim of keeping control by the founders and dominant shareholders, which becomes a crucial governance mechanism, particularly under the conditions of a weak legal system.

## Conclusion

Pyramidal structures are the specific form of ownership and control created with the use of cross shareholdings and multi level relations of companies. Pyramids are well known and quite popular in listed companies worldwide, particularly in emerging markets such as India, Korea, Latin America and continental Europe, mostly in Sweden, Belgium and Italy. The prime reasons for creating pyramidal structure is to maintain control over portfolio companies while lowering the capital involvement. Pyramids are traditionally used by founders and their families a company which in the process of growth and development becomes listed on the stock market. The form of a pyramid is often criticized by pro-investors and Anglo-Saxon practitioners since this ownership form is perceived as less transparent. Moreover, pyramids lead to the separation of ownership and cash flow rights and leave the control and decision making in the hands of the dominant shareholder. Comparative analysis reveals that the development of pyramids may lead to the expropriation of minority shareholders by the controlling investor via the transfer of the value and controversial party-related transactions within the corporate group. The analysis of 30 largest Polish listed companies confirm the ownership concentration as the most popular method of control and depicts the strong presence of pyramidal structures. According to the collected

evidence almost half of the largest companies listed on the Warsaw Stock Exchange adopt pyramidal structures which are controlled either by the strategic investor or an individual investors (founder and his/ her family). Undoubtedly, the identified phenomenon requires further research.

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### Abstract

The extensive research on corporate governance, economies' transition and strategic management delivers interesting and important insights into the characteristics of companies operating in different countries. The growing popularity of the comparative analysis approach also enriches management literature as it allows for extended studies on similarities and differences and dynamics of the patterns which companies follow with respect to both their operation and characteristics. Ownership structure with the reference to the comparative studies worldwide, types, forms and patterns identified in companies as well as the logic behind the behavior of different owners constitutes an important theme in management studies. The opportunity to confront forms found in different countries (with the reference to the degree of concentration and shareholder identity) and the dynamics of the current changes help understand the shifts in realized strategies, undertaken restructuring schemes, adopted organizational structures and implemented motivation or reporting frameworks. The paper presents the essential dimensions of ownership structure focusing on its specific form known as pyramids. It analyzes the reasons for creating and logic of functioning pyramidal structures and delivers a brief presentation of the pyramidal structures identified in Poland amongst the largest public listed companies.

**KEY WORDS: OWNERSHIP STRUCTURE, PYRAMIDAL STRUCTURE, CORPORATE GOVERNANCE, POLAND**

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## STRUKTURY PIRAMIDOWE W POLSCE

### Streszczenie

Badania z zakresu ładu korporacyjnego, transformacji gospodarek oraz zarządzania strategicznego dostarczają wielu cennych wniosków i obserwacji w zakresie charakterystyki przedsiębiorstw działających w poszczególnych krajach. Rosnące zainteresowanie analizami porównawczymi wzbogaca literaturę przedmiotu i pozwala na identyfikację różnic i podobieństw oraz dynamiki zmian zachodzących w odniesieniu do charakterystyki i strategii wielu różnych przedsiębiorstw. Jednym z zagadnień poruszanych w analizach porównawczych jest struktura własności, w szczególności różne jej wzorce, typy i formy. Poszczególne rozwiązania z zakresu struktury własności (stopień koncentracji, tożsamość akcjonariuszy) wywierają wpływ na logikę działania przedsiębiorstw na rynku i stanowią istotny wątek w analizach nauk o zarządzaniu. Możliwość skonfrontowania wzorców i dynamiki struktury własności zachodzących w poszczególnych krajach pomaga zrozumieć wdrażane zmiany, przeprowadzane programy restrukturyzacyjne, przyjęte struktury organizacyjne czy nawet konstruowane systemy motywacyjne. Niniejszy artykuł przedstawia różne wymiary struktury własności, koncentrując się na jej specyficznej formie, jaką są struktury piramidowe. Artykuł podejmuje także próbę przedstawienia logiki tworzenia i funkcjonowania struktury piramidy oraz prezentuje występowanie struktur piramidowych wśród największych spółek giełdowych w Polsce.

**SŁOWA KLUCZOWE: STRUKTURA WŁASNOŚCI, STRUKTURY PIRAMIDOWE, ŁAD KORPORACYJNY, POLSKA**