Hybridizing Investors: Designing Investment Organizations for Social Impact

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Abstract

Sustainable finance aspires to align capital markets with sustainability goals, yet remains criticized for its limited social impact. Prior research has largely examined investors' interactions with firms, overlooking the organizational design of the investment intermediaries that channel most financial capital. This study opens the "black box" of investment organizations by examining how asset owners and asset managers jointly design them to pursue both financial and social objectives. Building on a 16-month ethnography of a private equity impact fund complemented by interviews and archival data, we trace how these actors negotiate and stabilize the fund's organizational architecture (its value-creation objectives, resources, and governance and control structures) before it becomes active on the market. We identify three interrelated organizational mechanisms. First, locking the organizational architecture ex-ante mitigates agency costs and shapes the asset manager's subsequent behavior. Second, building a social impact ambition leads to hybridizing this architecture by coherently integrating financial and social logics. Third, the resulting configuration exerts a framing effect on investment and monitoring practices, channeling attention and decision-making toward aligned financial and environmental goals. By theorizing these mechanisms, the study builds the organizational foundations of both agency capitalism and sustainable finance. It conceptualizes sustainable finance as an organizational design problem under hybridity constraints, showing that due to financial intermediation, the social impact potential of sustainable finance is determined upstream in the investment chain (through the design of investment organizations) rather than downstream in the financial markets.

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1 Introduction

Over the past two decades, sustainable finance—the integration of environmental, social, and governance (ESG) criteria into investment decisions—has become mainstream. It promises to align the financial system with planetary boundaries and contribute to addressing contemporary grand challenges by delivering social[1] outcomes alongside financial returns. Since the launch of the UN-backed Principles for Responsible Investment in 2006, the number of signatories has grown from 63 institutional investors to over 5,000, now representing more than $128 trillion in assets under management as of March 2025. Despite this substantial growth, experts, academics, and policy makers question whether these practices are mere greenwashing or produce real social impact (Edmans, 2023; Gosling & Walkate, 2024), even for the most ambitious impact investing strategies (Schlütter et al., 2023). For instance, BlackRock's former Head of Sustainable Investing declared in 2021: *"We are at a moment in history when skepticism on ESG products is extraordinary. Journalists, fund managers, everyone is quietly talking about it. The major problem that I have is that even if they're marketed correctly [ESG funds], they actually have no demonstrable impact."*[2] A few months later in Germany, police officers and investigators raided the offices of DWS (an asset manager affiliated with Deutsche Bank) in a fraud investigation because of alleged "greenwashing" regarding their use of ESG criteria in investment decisions, ultimately costing the CEO's job and a €27m fine.[3]

Prior research on sustainable finance has focused on the mechanisms through which investors can influence firm behavior and drive a positive social impact: allocating capital based on extra-financial criteria (Heinkel et al., 2001; Oehmke & Opp, 2025; Pástor et al., 2021) and actively engaging companies using shareholder rights to promote sustainable practices (Chuah et al., 2024; Dimson et al., 2015; Goranova & Ryan, 2014). However, this work focuses on the relationships between firms and their investors, implicitly treating the latter as atomistic and rational actors. Yet, our financial system is heavily intermediated by multiple layers of organizations that manage capital on behalf of beneficiaries, such as institutional investors (Aguilera et al., 2025), creating additional agency issues (Jensen & Meckling, 1976) in the financial markets[4]. These organizations are highly heterogeneous (Goranova & Ryan, 2022) and their behavior is framed by the mandates negotiated with their beneficiaries. This intermediation not only multiplies agency problems (Fisch, 2010) but

[1] We use "social" in a broad sense, including both environmental and social issues.

[2] https://trellis.net/article/blackrocks-former-head-sustainable-investing-says-esg-and-sustainability-investing-are/

[3] https://www.reuters.com/business/finance/former-dws-ceo-woehrmann-suspect-greenwashing-probe-handelsblatt-2023-07-07/

[4] This phenomenon is often referred to as *agency capitalism* (Gilson & Gordon, 2013).

also transforms our financial system into a network of organizations whose behavior may depend on their individual design (Simon, 1976). While law and economics research has examined the incentives and constraints embedded in investment mandates (Bebchuk et al., 2017; Gilson & Gordon, 2013), it still treats institutional investors as "black boxes" responding to these incentives, overlooking how their organizational design may also shape their behavior.

Building this organizational perspective seems important for institutional investors engaging in sustainable finance. Indeed, as for any organization, integrating a social dimension alongside financial returns in the objective function of institutional investors leads them to gradually become hybrids (Battilana et al., 2017), combining multiple institutional logics (Thornton & Ocasio, 1999). This creates potential tensions with their stakeholders (in our context, increased agency costs) and internal coordination problems. These tensions, if unaddressed by the organization's design, can lead to *mission drift* (Ebrahim et al., 2014) when one logic (e.g., the financial logic) overpowers the other (e.g., the social logic), and ultimately undermines their ability to deliver the intended dual performance. The governance structure, for example, has been identified as a key organizational component that allows hybrid organizations to navigate competing logics (Battilana et al., 2022) and protects hybridity over time (Mair et al., 2015). While these studies highlight how organizational arrangements can help sustain hybridity, we still lack a systematic understanding of how such design processes unfold in the context of investment organizations, due to the sector's structural opacity (Radin & Stevenson, 2006). In sustainable finance, this question is particularly salient: the effectiveness of sustainable investors' strategies may depend not only on the market mechanisms they use (Broccardo et al., 2022) or their external incentives (Lowry et al., 2025), but also on how investment organizations are structured to accommodate multiple institutional logics over time and foster systematic practices leading to social impact.

Building on this premise, we adopt an organizational design perspective (Burton & Obel, 2004; Joseph & Sengul, 2025; Siggelkow, 2011) to study how investment organizations are designed. Specifically, we ask: How can asset owners and asset managers design investment organizations that systematically deliver both financial and social returns? Moving away from the interactions between investors and their portfolio companies, we open the "black box" of investment organizations by studying their structuring through the upstream interactions between asset owners and asset managers, and how these organizations can subsequently frame their behavior. To explore this question, we build on an inductive longitudinal case study (Yin, 2009) of a private equity impact investing fund focused on environmental transition. We collected data through a 16-month ethnography (between September

2022 and March 2024) directly within the asset manager's team, conducted 12 interviews (with the asset manager and its asset owners), and analyzed archival documents. Such data on a private equity fund are particularly original due to confidentiality concerns and a lack of transparency in this sector (Abraham et al., 2024; Phalippou et al., 2018).

Private equity impact investing provides an appealing empirical context (Eisenhardt & Graebner, 2007; Siggelkow, 2007) for addressing our research question for two reasons. First impact investors are the most ambitious sustainable investors (Busch et al., 2021) and likely to drive social impact, since they explicitly target financial and social returns (Höchstädter et al., 2015). Second, the private equity asset class is almost entirely intermediated by multiple layers of professional organizations (Sahlman, 1990), which are used to design complex mechanisms to reduce high agency issues (Jensen, 1989). It also has a high potential for social impact, as private equity investors have a long-term orientation and significant control, enabling them to exert considerable influence over portfolio companies (S. N. Kaplan & Stromberg, 2009).

Our analysis reveals two interrelated organizational mechanisms through which asset owners and asset managers jointly design investment organizations capable of pursuing financial and social objectives. First, we identify a *locking* mechanism that stabilizes the fund's organizational architecture for its whole life-cycle. During the negotiation of the mandate between asset owners and asset managers, they define and fix some of the fund's key organizational components (its objectives, resources, governance and control structures) to mitigate agency costs that may arise during its active life. Consistent with organization design literature (Joseph & Sengul, 2025), the resulting architecture has a *framing* effect on the asset manager's market behavior, influencing how they process information, coordinate, and make decisions. Second, and in line with previous literature on hybrid organizing (Battilana et al., 2017), we document that investors developing sustainable finance strategies *hybridize* this organizational architecture. They integrate the financial and social logics into every component of the fund's organizational architecture, ultimately achieving a high level of fit (Siggelkow, 2002) to foster subsequent investment and monitoring practices aimed at dual performance. These two mechanisms jointly explain how sustainable investment organizations can be designed ex-ante to deliver social impact through their activities.

By theorizing these mechanisms, this study makes two main contributions. First, it extends the notion of agency capitalism (Bebchuk et al., 2017; Gilson & Gordon, 2013) by building its organizational foundations, that is, the ex-ante design choices through which investors manage the agency costs of intermediation and shape their own behavior. By acknowledging the organizational nature of

institutional investors, who own most of today's firms, our findings support the claim that shareholders are not a homogeneous group (Goranova & Ryan, 2022) and give a simple framework to analyze their heterogeneity based on their organizational architectures. This provides a new perspective on the long-standing debate about "shareholder supremacy" (Freeman et al., 2004; Jensen, 2001; Stoelhorst & Vishwanathan, 2024) and the recent developments regarding the purpose of firms (George et al., 2023). As shareholders are mainly organizations, their design could be modified to represent key stakeholders (McGahan, 2023a) and ultimately protect their interests through traditional shareholder rights and corporate governance mechanisms (Edmans & Holderness, 2017). By detailing how a private equity asset manager did so for the environment, this study makes a first step in this direction. Second, this study advances prior research on sustainable finance and impact investing (Kölbel et al., 2020; Marti et al., 2024; Schlütter et al., 2023) by grounding it as an organizational design problem (Burton & Obel, 2004). We conceptualize sustainable finance as the design of investment organizations under conditions of hybridity (Battilana & Dorado, 2010), where multiple institutional logics (financial and social) must be integrated coherently within the same architecture. The social impact potential of sustainable finance practices depends on how investment organizations are structured before entering the market, as this architecture shapes their subsequent behavior and capacity to sustain dual objectives over time. This shifts the analytical focus from the interactions between companies and investors to the internal structure of investment organizations themselves, emphasizing the central role of asset owner–asset manager interactions in this structuring process (Edmans et al., 2024). Prior research has identified important isolated organizational components of impact investors, such as contracts and incentives (Geczy et al., 2021; Thirion et al., 2022), business model structuring (Bandini et al., 2022), or impact management and measurement systems (Kaufmann et al., 2025). Building on organizational design theories (Joseph & Sengul, 2025), particularly configurational (Miller, 1996) and control (Cardinal et al., 2017) approaches applied to hybrid organizing (Battilana et al., 2017), we integrate these elements into a coherent framework for analyzing the organizational architecture of investment organizations engaging in sustainable finance. This framework defines the various levels of social ambition among investors as different degrees of hybridization of objectives, which must be matched by a consistent hybridization of the entire organizational architecture to ensure internal fit (Siggelkow, 2002) and foster investment practices aligned with those ambitions. More broadly, this perspective provides the organizational foundations of sustainable finance, allowing any investor to be analyzed through the lens of its design choices under hybrid constraints.

While our analysis focuses on the private equity industry, a context characterized by high agency

costs and dense intermediation among professional organizations, the mechanisms we identify are not confined to this setting. They stem from the very process of financial intermediation, in which decision rights and preferences are delegated across multiple layers of investors, and are thus likely to occur in other asset classes. Moreover, these mechanisms are particularly important to understand because they operate repeatedly along the entire investment chain: most asset owners are themselves asset managers investing on behalf of other principals, up to the individual beneficiaries at the end of the chain.

The rest of the paper is organized as follows. Section 2 presents the related literature on sustainable finance, hybrid organizations, and corporate governance. Section 3 describes our key methodological choices. Section 4 presents our findings through Gioia et al. (2013) data structures and a complete processual model. Section 5 develops our theoretical contribution, providing the organizational foundations of both agency capitalism and sustainable finance. We conclude in section 6 by giving the managerial and policy implications of our results, as well as the limits of this work and potential avenues for future research.

2 Related Literature

This section reviews the literature on sustainable finance, agency capitalism, and organizational design. Research on sustainable finance has primarily examined how investors influence corporate behavior through capital allocation and shareholder engagement. Yet most of the capital in financial markets is managed by institutional investors acting on behalf of beneficiaries, creating an additional layer of intermediation and agency issues. These intermediaries are not atomistic actors but complex organizations whose internal features shape how they behave on the market. However, existing research on agency capitalism largely models these intermediaries as incentive-driven "black boxes," overlooking their organizational characteristics. Addressing this gap requires reconnecting the study of sustainable finance and agency capitalism with insights from organizational design theory, which illuminate how the configuration of internal organizational components shapes subsequent behavior. We therefore review this stream of research to discuss its analytical implications for understanding investment organizations and the development of sustainable finance strategies.

2.1 Sustainable finance mechanisms: (re)allocating capital and engaging companies for social impact

Sustainable finance relies on two complementary strategies to influence corporate behavior: capital allocation and shareholder engagement (Kölbel et al., 2020).

Capital allocation strategies direct financial flows toward or away from specific assets based on environmental, social, and governance (ESG) criteria. These include exclusion practices that penalize firms through progressive divestment, tilting strategies that favor the most sustainable firms within each industry, and impact investing that specifically targets companies addressing social challenges. Extensive theoretical work has been conducted to assess the potential market equilibrium and social welfare impacts of these practices. It demonstrates how capital reallocation based on ESG criteria can affect firms' cost of capital at equilibrium, creating an incentive for pro-social behavior and potentially improving social welfare (Heinkel et al., 2001; Oehmke & Opp, 2025; Pástor et al., 2021). It thus depends on the share of responsible investors on the market, their willingness to pay for sustainable assets, and the cost for firms to reform their activities. Exclusion practices can alter risk-sharing at equilibrium and increase the cost of capital for excluded firms by shrinking their investor base (Heinkel et al., 2001), creating an incentive for firms to adopt pro-social practices. Instead of excluding sin stocks, investors can also tilt their portfolio towards the most sustainable assets in each industry for moral reasons or to hedge extra-financial risks (Capelle-Blancard & Monjon, 2014), leading to a lower cost of capital for green assets (Pástor et al., 2021). By accepting lower returns and considering social costs, responsible investors can help scale clean production capacities and enhance social welfare, especially when financial constraints are high and clean technology has lower profitability (Oehmke & Opp, 2025). Empirical evidence offers partial validation of these theoretical predictions. Pioneering work supports the claim that investors have extra-financial preferences that affect asset prices (Flammer, 2013) and companies' cost of capital (Chava, 2014). Sin stocks tend to be excluded from institutional investors' portfolios and outperform peers (by 2.5%-3% per year), suggesting underpricing due to limited demand (Hong & Kacperczyk, 2009), and shocks in ESG preferences drive the returns of green assets (Pástor et al., 2022). Similarly, in other contexts, sustainable finance instruments such as green bonds (Flammer, 2021; Zerbib, 2019) and venture capital impact funds (Barber et al., 2021) also exhibit lower returns, reinforcing the claim that investors are willing to sacrifice financial returns for social benefits. The growing practice of blended finance (Flammer et al., 2025a, 2025b) demonstrates how investors accepting lower returns can alleviate financial constraints

and help scale sustainability-oriented projects, especially in emerging markets. Still, recent studies on the US stock market reveal mixed effects of this mechanism on social welfare. The change in firms' cost of capital appears to be too narrow to trigger a significant reaction by firms (Berk & van Binsbergen, 2025). For instance, green firms become greener with additional capital at a slower pace than brown firms become browner with less capital, inducing a counterproductive effect of these practices (Hartzmark & Shue, 2022).

Given the limitations of this first strategy, some investors engage directly with companies, using their formal powers (voting, filing resolutions, and filing lawsuits) and informal powers (private negotiations and institutional influence) as shareholders to influence corporate behavior (Goranova & Ryan, 2014). Chuah et al. (2024) provides a comprehensive cross-disciplinary review of the engagement process, decomposed into three steps: target identification, engagement approach & the dynamics of negotiation between shareholders and top managers, and the measurement of firm-level outcomes. This process is depicted as complex (involving diverse stakeholders whose reactions might influence the outcomes, such as NGOs, the media, and other stakeholders), dynamic (often repeated with feedback loops), and adaptive (each actor adapting its tactics and actions to maintain the status quo or drive change in corporate behavior). Activists generally target large underperforming firms (Dimson et al., 2015), for which the issues raised are very material or drive reputational concerns (Barko et al., 2021). Collaboration between activist shareholders in coalitions is a key determinant of engagement's success (Dimson et al., 2021), which often takes the form of a two-level coalition (Brav et al., 2021) with a lead investor actively negotiating with the firm, while being supported by a group of other investors providing expertise, legitimacy, and influence. Tailoring coalitions (size, identity of the lead) according to the issues addressed and the characteristics of the target (financial materiality of the issue, size, location) can significantly increase the success of the engagement (Slager et al., 2023). The outcomes of such engagement are generally positive as it increases ESG scores (Barko et al., 2021), enhances voluntary disclosure (Flammer et al., 2021), lowers portfolio downside risk (Hoepner et al., 2021), and generates a positive market reaction (Barko et al., 2021; Dimson et al., 2015; Flammer et al., 2021).

Overall, while these sustainable finance strategies have gained traction, their effectiveness in producing social impact remains uncertain (Gosling & Walkate, 2024), even for impact investing (Schlütter et al., 2023). For example, despite growing environmental commitments, there is a disconnect between the decarbonization path of institutional investors and the global decline in GHG emissions (Atta-Darkua et al., 2023). Broccardo et al. (2022) theoretically compare the effectiveness of capital

allocation and shareholder engagement in achieving social welfare optima. The first acts as a "subsidy" for firms and only reaches the optimum when strong pro-social preferences are widespread among investors, which is empirically unlikely. In contrast, shareholder engagement acts like a more effective "tax" (voted reforms apply to every investor) and leads to the social welfare optimum when only a majority of investors hold weak but non-zero pro-social preferences, as the private cost of reforming firms borne for diversified investors is always lower than the utility derived from the social benefit. Still, modern SRI funds are mainly "stock pickers" who select firms with better environmental and social performance, but do not improve it after investing (Heath et al., 2023) or invest in improving firms, potentially leading to a low impact on social welfare.

This body of work identifies the levers available to investors to influence corporate behavior and potentially yield a positive social impact (Marti et al., 2024), and documents the conditions under which they can be effective. Yet, this literature focuses on interactions between investors and firms in the financial markets, implicitly treating investors as unitary and rational actors. In practice, most capital is channeled through institutional investors (such as pension funds, hedge funds, mutual funds, and other types of asset managers), which are complex organizations managing capital on behalf of ultimate owners.

2.2 The rise of agency capitalism and the implications for sustainable finance

Today's financial system is heavily intermediated by institutional investors, which collectively own the vast majority of equity holdings. In the United States, they own over 80% of S&P500 companies (Hart & Zingales, 2022), and just three of them (namely BlackRock, Vanguard, and State Street) own more than 20% of S&P500 stocks and are collectively the largest shareholder in 88% of these firms (Aguilera et al., 2025; Bebchuk & Hirst, 2019). This concentration represents a shift from dispersed individual ownership (Berle & Means, 1991) toward intermediated ownership through professional organizations. Scholars (especially from law and economics) have long recognized that this intermediation dilutes the monitoring role of shareholders by creating a second layer of agency issues (Fisch, 2010) further decoupling ownership and control of firms, as these organizations value liquidity and diversification over control and costly involvement in governance (Coffee, 1991; G. F. Davis, 2008). The concept of shareholders as rational and unitary owners is thus outdated, yielding significant implications for capital markets and corporate governance (Goranova & Ryan, 2022): shareholders' interests are heterogeneous, and long intermediation chains decouple residual risk-bearing & control rights, ultimately

affecting their behavior on the market.

Bebchuk et al. (2017) introduces the concept of *agency cost of institutional ownership* by modeling the fee structures of these actors and predicting their effects on monitoring activities. A typical institutional investor holds a diversified portfolio of stocks and charges a fee as a percentage of its assets under management (AuM). If they engage in monitoring and increase a firm's value, they bear all the private costs of monitoring while capturing only a small fraction of the benefits through their fees. Competition among institutional investors partially enhances the incentive to engage in active ownership, as financial flows are driven by relative performance (compared to an index or other active funds), and the benefits of stewardship are shared among all institutions. It thus only creates an incentive to engage in monitoring activities for active managers who overweight the targeted firm in their portfolio compared to the index. Overall, because institutional investors have diversified portfolios and low performance-related compensation, they tend to undervalue governance rights compared to traditional shareholders (Gilson & Gordon, 2013). Some institutional investors, such as hedge funds, contribute to addressing this governance gap as they have a high performance-related compensation, creating an incentive to engage in stewardship activities (Lewellen & Lewellen, 2022)[5].

This economic perspective treats institutional investors primarily as "black boxes" reacting to economic incentives, focusing on how fee structures and diversification affect behavior (Bebchuk et al., 2017; Gilson & Gordon, 2013; Lewellen & Lewellen, 2022) while neglecting their internal organizational dynamics. Fisch (2010) noted that "In short, the modern institutional investor itself functions much like the Berle & Means Corporation", and is subject to agency and coordination issues. Recent empirical evidence also reveals substantial heterogeneity in institutional investor preferences and behaviors that cannot be fully explained by economic incentives alone. McCahery et al. (2016) survey institutional investors and find significant variation in governance preferences, engagement strategies, and willingness to sacrifice returns for governance improvements—variation that correlates with organizational characteristics rather than just fee structures or portfolio concentration. This organizational heterogeneity is further demonstrated by DesJardine et al. (2023), who develop a typology of institutional investors based on investment horizon and value-creation orientation. They identify four distinct types: Transactional (short-term, financially focused), Durable (long-term, financially focused), Purpose-Driven (short-term, multi-purpose), and Sustainable (long-term, multi-purpose). Each type exhibits different motivations, combines traditional mechanisms (exit, voice, and provid-

[5]In 2017, the typical institution generated $129,000 ($84,400 through direct fees, $44,600 through additional flows) in extra annual fees from a 1% rise in firm value consequent to engagement (Lewellen & Lewellen, 2022). As predicted, the relative incentive is significantly higher for activist investors, such as hedge funds (32% of AuM), compared to index funds (0.56% of AuM).

ing resources) in distinct ways, and ultimately has a distinct impact on stakeholders. This typology demonstrates that institutional investors' behavior cannot be understood solely through economic incentives, as other organizational characteristics play crucial roles in determining their market behavior. While we begin to understand the consequences of different organizational forms of investors (Brav et al., 2008; Chuah et al., 2024; DesJardine et al., 2021, 2023), there is much to learn about the process through which institutional investors develop their organizational architecture, and how it may ultimately affect their behavior.

This organizational perspective seems even more relevant in the context of sustainable finance. Such investors, who are progressively integrating ESG factors into their value-creation objectives, are becoming increasingly hybrid organizations (Battilana et al., 2017; Yan et al., 2021): entities that pursue both financial and social objectives simultaneously. Growing evidence demonstrates this shift: institutional investors increasingly integrate ESG factors into their investment decisions for both financial and moral reasons (Dyck et al., 2019; Krueger et al., 2020; Riedl & Smeets, 2017), with Hart and Zingales (2022) documenting how shareholders now routinely push companies toward actions that may reduce market value but advance environmental and social goals. This dual-objective pursuit raises fundamental questions of organizational design: how can institutional investment organizations configure their internal architectures to durably pursue both financial and social goals without falling "into mission drift", which often plagues hybrid organizations (Ebrahim et al., 2014)? Understanding these organizational mechanisms is thus crucial for assessing and unleashing the potential of sustainable finance to generate social impact at scale.

2.3 The organization design perspective of institutional investors

Institutional investors are complex organizations whose behavior and performance are fundamentally shaped by their design choices (Joseph & Sengul, 2025). For example, building on Sah and Stiglitz (1986)'s work on decision-making structures, Csaszar (2012) demonstrates that the organizational architecture of mutual funds, in terms of centrality (i.e., the number of decision makers and the consensus threshold), affects their capital allocation choices and ultimately their performance. Siggelkow (2002) documents, in turn, how Vanguard's success stems from strong complementarities among organizational elements.

Drawing on the behavioral theory of the firm (Cyert & March, 1963), we consider organizations as formal structures of coordination that allow collective action and the pursuit of joint goals among members with bounded rationality (Simon, 1957) and potentially conflicting interests. They

are fundamentally information-processing systems that transform uncertainty into coordinated action (Galbraith, 1977). In this perspective and as any organizations, institutional investors can be viewed as activity systems (interdependent sets of objectives, policies, capabilities, controls, structures) that require careful configuration to achieve internal fit (Burton & Obel, 2004; Rivkin & Siggelkow, 2003; Siggelkow, 2011), when each component complements each others, reinforcing organizational coherence and ultimately performance (Siggelkow, 2002). Within this architecture, control structures are pivotal, aligning individual behavior with organizational goals while mitigating the costs of delegation (Cardinal et al., 2004; Fama, 1980; Jensen & Meckling, 1976). They also shape cognition by building routines (S. Kaplan & Henderson, 2005) and channeling attention to specific issues (Ocasio, 1997). For institutional investors, whose business revolves around screening opportunities and monitoring portfolio firms in uncertain environments on behalf of their asset owners, these information-processing demands and control mechanisms are especially acute. This makes configuration (Miller, 1996) and control (Cardinal et al., 2017) approaches particularly relevant, since both directly address how organizations are designed to allocate attention and resources, process information, and align actions to strategic objectives.

Beyond internal coherence, organizational performance also depends on external fit, the alignment between an organization's structure and environmental constraints (Burton & Obel, 2018). Classic contingency theory argued that no single design is universally optimal, as performance depends on matching internal arrangements to external contingencies such as task uncertainty or environmental turbulence (Donaldson, 2001; Lawrence & Lorsch, 1967; Van De Ven et al., 2013). Neo-institutional theorists also stress that organizations must align with prevailing norms and expectations in their field to gain legitimacy and secure resources, often adopting isomorphic practices perceived as appropriate, even if not the most efficient (DiMaggio & Powell, 1983; Meyer & Rowan, 1977).

From this institutional perspective, investment organizations developing sustainable finance strategies can be characterized as hybrid organizations (Battilana et al., 2017), combining market-driven financial logic[6] with socially motivated goals (Yan et al., 2021). Combining institutional logics creates external and internal tensions due to potential trade-offs (Battilana, 2018), such as balancing conflicting institutional expectations (e.g., financial returns from investors and social impact from other stakeholders), difficulties in measuring organizational performance, and individual value clashes that potentially lead to legitimacy deficit and resource constraints. These pressures can create a mis-

[6] An institutional logic is the set of material practices and symbolic systems including assumptions, values, and beliefs by which individuals and organizations provide meaning to their daily activity, organize time and space, and reproduce their lives and experiences (Thornton et al., 2012).

sion drift (Ebrahim et al., 2014), when one logic ultimately overpowers the other, and in the case of sustainable finance, undermines the social impact potential of these investors. To mitigate this risk, hybrid organizations often engage in selective coupling (Pache & Santos, 2013) and develop forms of structured flexibility (Smith & Besharov, 2019) to integrate practices from both logics, thereby satisfying stakeholders' expectations without compromising their core mission. In sustainable investment organizations, this selective coupling can manifest in reconciling rigorous financial performance metrics with softer environmental or social impact assessments (Arjaliès & Bansal, 2018). Organizational governance structures are the final key mechanism allowing organizations and individuals to navigate multiple institutional logics over time by enabling internal and external legitimacy building (Ebrahim et al., 2014; Mair et al., 2015). Several governance bodies, such as boards, serve as spaces for negotiation (Battilana et al., 2015) to arbitrate between conflicting expectations (Pache et al., 2024). These mechanisms act as filters of institutional pressures (Battilana et al., 2022) by explicitly accounting for the trade-offs inherent to dual-purpose organizations, allowing them to maintain their commitment to the multiple logics and achieve their mission effectively.

Governance "defines the end toward which the organization is directed, the people who make key decisions, the means employed to achieve this end" (Battilana et al., 2022). It answers three key organizational questions: toward which stakeholder does the organization aim to create value (Freeman et al., 2004; Jensen, 2001; Klein et al., 2019; McGahan, 2023b), how to align key stakeholders to these value-creation objectives (Bridoux & Stoelhorst, 2022), and how to control top managers based on their hypothetic behavior (opportunistic (Jensen & Meckling, 1976) or altruist (J. H. Davis et al., 1997)). It involves allocating property rights (Alchian & Demsetz, 1973) that vary depending on the type of issues encountered (Foss & Klein, 2018; Stoelhorst & Vishwanathan, 2024). Through these mechanisms, governance reduces agency costs (Dalton et al., 2007; Hill & Jones, 1992; Jensen & Heckling, 1995; Jensen & Meckling, 1976) while filtering institutional pressures (Battilana et al., 2022), enabling organizations to balance performance, legitimacy, and impact over time.

Despite the organizational nature of institutional investors and this theoretical background on organizational design, our understanding of how they are structured and governed remains limited due to the sector's opacity (Radin & Stevenson, 2006). Recent scholarship has begun to examine some organizational components of investors engaging in sustainable investing. In a survey of 509 fund managers, Edmans (2024) finds that the actions of sustainable investors are largely driven by the mandates and constraints set by asset owners. In the context of impact investing, Thirion et al. (2022) highlight how asset owners and managers co-construct impact objectives and incentive

schemes that "lock in" the social mission at the fund level. Kaufmann et al. (2025) demonstrate that impact measurement often functions less as a performance management tool than as a relational mechanism between asset owners and managers, driving legitimacy. Bandini et al. (2022) explore the business models of impact funds and argues that the impact proposition must be embedded throughout organizational practices. Finally, Geczy et al. (2021), studying 53 impact funds, show that only a minority (13%) incorporate impact-related incentives or impact committees (9%) in their contracts. Taken together, these studies highlight important isolated components of investment organizations operating sustainable finance strategies, but they remain partial and disconnected.

2.4 Toward an organizational perspective on sustainable finance

To synthesize, prior research on sustainable finance has extensively studied how investors use market-based and governance mechanisms to influence corporate behavior and generate social impact (Kölbel et al., 2020; Marti et al., 2024). Yet these mechanisms are fundamentally mediated by institutional investors (Goranova & Ryan, 2022), who manage capital on behalf of asset owners. This intermediation introduces well-documented incentive distortions (Bebchuk et al., 2017; Gilson & Gordon, 2013; Lewellen & Lewellen, 2022) that shape investors' behavior in financial markets. While institutional investors are fundamentally complex organizations, and while extensive organizational design literature provides frameworks for understanding how organizations coordinate collective action and pursue multiple objectives (Battilana et al., 2017; Joseph & Sengul, 2025), these theoretical streams remain disconnected: organizational design principles have rarely been applied to understand how institutional investors are structured and governed. This disconnect is particularly consequential in the context of sustainable finance, where institutional investors increasingly pursue dual financial and social objectives that are often weakly correlated or even conflicting in the short term (Ethiraj & Levinthal, 2009). As they become hybrid organizations (Battilana et al., 2017), sustaining this dual purpose over time requires precise organizational configuration to manage inherent tensions rising with hybridity (Battilana, 2018; Mair et al., 2015). We thus still lack understanding of how investment organizations are structured through asset owner–asset manager interactions, how these formation processes condition subsequent market behavior, and how their organizational architectures should evolve to embed social impact alongside financial returns. While recent studies examine isolated elements, such as contracts, incentives, or measurement systems (Bandini et al., 2022; Geczy et al., 2021; Thirion et al., 2022), we need an integrative framework that provides the organizational foundations for both agency capitalism and sustainable finance.

3 Methods

3.1 Research context: a private equity impact investing fund focused on environmental issues

We use the private equity impact investing sector to investigate our research question as it is an appealing context (Eisenhardt & Graebner, 2007; Siggelkow, 2007) in which to study the design and governance of investment organizations targeting social impact. Impact investors explicitly target financial and social returns systematically (Höchstädter et al., 2015) and are, in theory, the most likely to drive social impact (Busch et al., 2021). While this practice recently reached the $1tr AuM milestone and is growing rapidly (Hand et al., 2022), it still suffers from impact-washing claims (Findlay & Moran, 2019) as there is no clear evidence of its final real-world impact (Schlütter et al., 2023). Choosing the private equity (PE) asset class is natural as it has a high social impact potential and represents 65% of global impact investing AuM (Hand et al., 2023). PE plays a crucial role in our economies by supporting private companies, such as start-ups and SMEs, some of which are trying to solve a social problem (impact-native companies) (Barber et al., 2021). PE investors typically have fixed holding periods (generally between 4 and 7 years) and greater proximity with management teams compared to investors of listed firms (S. N. Kaplan & Stromberg, 2009). This allows them to influence companies' behavior and drive sustainable value creation by aligning long-term business strategies with sustainability objectives, a critical factor in the success of shareholder engagement (Barko et al., 2021; Dimson et al., 2015). Finally, private equity is relatively illiquid, and most funds are structured as limited partnerships with a 10- to 12-year life. To keep their liability limited, asset owners must not intervene in fund management operations and thus rely on rigorous governance schemes tailored by professionals at the fund's inception to influence and monitor the behavior of asset managers (Sahlman, 1990). For all these reasons, impact investing strategies in private equity represent a natural context to study the design and governance of investment organizations aiming to yield social impact (Eisenhardt & Graebner, 2007; Siggelkow, 2007).

After performing desk research and interacting with many PE firms in France[7] from 2020 to 2021, we chose to study the case of an impact fund focused on environmental issues in May 2022. This strategy was coined in 2020, and the firm had just started pitching to asset owners. We present the

[7]While the choice of the French context is rather opportunistic, it is nevertheless promising as Europe is leading the worldwide regulation of sustainable finance with the *Green Deal (SFDR, Taxonomy)*, and the French private equity industry is one of the most active in Europe.

main characteristics of the fund in Table 4. We chose this case for four main reasons:

- It complies with the modern definition of impact investing (social and financial returns targets),
- It combines shareholder engagement processes (helping SMEs decarbonize their activities) with screening strategies (investing in decarbonizing assets) to deliver the targeted social impact and is thus representative of the spectrum of sustainable finance mechanisms,
- It focuses on environmental issues, for which there are advanced accounting and target-setting frameworks (e.g., GHG Protocol and SBTi),
- It presents an innovative governance scheme incorporating the environmental objectives: carried interest is linked to impact targets, and an independent impact committee monitors the investment activities.

During our data collection process, we observed +60 investment analysis processes, the fundraising process (pitches, due-diligence meetings, contractual negotiations), and one monitoring process focused on decarbonizing the operations of a portfolio company. A complete timeline of the events observed during our data collection is available in Figure 1. We also describe the key characteristics of the fund (investment strategy, impact management & measurement methodology, governance, and resources) in the onlice Appendix.

3.2 Data collection

We draw on three sources of primary data: participant observation, semi-structured interviews, and archival work. We provide a precise data summary in the appendix (Table A).

Participant observation. One of the authors was a junior analyst in the fund manager's team for 16 months (September 2022 to March 2024) dedicated to the impact investing strategy, comprising four people. This author was directly exposed to (and participated in) every debate and conversation, enabling him to gather precise, firsthand insights into the fund manager's team's perspective. This allows us to draw on more than 130 hours of participant observation in formal meetings and at least as much of informal discussions, meetings, and personal experiences. He was actively[8] involved in the operational and financial structuring of the fund, +60 investment opportunity analyses, and one company monitoring process. The first author also attended a series of Field Configuring Events (FCEs) gathering private equity professionals. The other author was part of the independent com-

[8]Regarding reflexivity, the first author had no decision power. The senior partners had already defined the investment strategy and its main characteristics when we entered the field. We are thus confident that we would have observed the same results if another junior had participated.

mittee supervising the fund's impact methodology, which met twice during the data collection period and continues to meet regularly. We collected data directly by taking precise notes of every formal meeting and brainstorming/debriefing discussions. The authors regularly shared their information to get the same level of understanding and elaborate on the data analysis. At the end of this field data collection, the authors synthesize their field notes in memos.

Interviews. We also performed open and semi-structured interviews with the asset manager and several asset owners to gain their perspective on the events, which were recorded (4) or during which we took precise notes (8):

- 8 open interviews (one every 6 to 8 weeks) with the senior partners of the investment team to formally reflect on the events of the periods [9],
- 2 semi-directed interviews with the asset manager's executives,
- 2 semi-directed interviews with asset owners that invested in the fund. These are the two corner investors of the fund who carried out in-depth due diligence and contractual negotiation.

While we discussed the specific events related to our case during the interviews, we also focused on the interviewees' overall experience with sustainable finance in the private equity industry, allowing us to build the external validity of our results.

Archival work. We had access to internal documents describing the fund strategy & governance, investment opportunities analyses, and monitoring processes. This includes legal, marketing, operational documents, and meeting minutes.

These multiple sources allowed us to obtain fine-grained data on the case from the key actors' perspectives and triangulate our results. This is particularly original in the private equity industry, reputed for its lack of transparency (Abraham et al., 2024; Phalippou et al., 2018).

3.3 Data analysis

We built our analysis by cycling back and forth between data and theory, following established guidelines in inductive analysis and grounded theory building (Gioia et al., 2013; Langley, 1999). We entered the field with a naive eye regarding our research question, as we initially planned to study shareholder engagement processes in the private equity industry. While our final research question and the organizational case of the asset management industry have remained largely unexplored so far (Bebchuk et al., 2017; Radin & Stevenson, 2006), we believe existing theories could enlighten our

[9] Focus on the precise events (related to fundraising, fund structuring, investment, and monitoring) we observed.

data collection and analysis. We thus adopted an abductive position by engaging deeply with the literature during our data analysis, aligning a rigorous positivist perspective during our data collection with an interpretative approach during the coding by going back and forth between the data and theory. We presented the resulting theoretical constructs as a Gioia et al. (2013) data structure, with multiple related second-order themes highlighting this interpretative process. The coding process was iterative, and we present the key steps that led to our results below. Both authors were involved at every step of this process, especially during coding.

Narrative accounts: establishing profiles & process bracketing. We started by writing a narrative account of our case (Langley, 1999). This was essential to building our analysis by consolidating our multiple data sources (especially given the primacy of participant observation data), the authors' different perspectives, and due to the technical complexity of our research context. We identified the key organizational components of an investment fund: the investment strategy, the resources used to deliver it, and the control & governance mechanisms used to influence the asset manager's behavior. Then, we characterized the profiles and interests of the actors involved in the life of an investment fund: the asset manager (AM), the asset owners (AOs), and the portfolio companies. This part of the narrative sensitized us to the importance of agency issues in the asset management industry. We also derived from this first step the key processes composing the life of an investment fund:

- **Creation & Strategy Development:** refers to the asset manager's development of the investment fund. They define the investment strategy and the main resources (team, processes, frameworks, external advisors) needed to deliver it.
- **Fundraising:** the asset manager starts selling its product to potential asset owners. They conduct in-depth due diligence before investing in the fund and engage in intensive legal negotiations to protect their interests throughout the fund's life. After reaching a certain amount of money raised (generally 60% of the fund target), the fund is "closed", allowing the asset manager to call and invest the money raised.
- **Investment:** the asset manager generates a "deal-flow" (i.e., a set of investment opportunities). It could be companies seeking funding for operational projects or shareholders willing to sell their stakes. The asset manager invests after in-depth due diligence (financial, legal, strategic, etc.). It structures and negotiates the transaction (financial instruments, governance representation, incentives) to maximize the value-creation potential for the fund.
- **Monitoring:** After investing, the asset manager monitors the managers of the portfolio com-

panies and helps them develop their business (e.g., bring commercial opportunities, help with new operational developments, external growth, etc.) before selling it after 4 to 7 years.

A fund's life ranges from 10 to 12 years in the private equity industry once it becomes active on the market (i.e., after the first closing). While the first two processes naturally happen before the last two, there is an overlap during the fund's fundraising process. The asset manager has to show that it can generate a deal flow that aligns with the strategy and analyze and execute transactions. Thus, the asset manager starts transactions during this period while raising funds from potential asset owners. We observed this period during our data collection, allowing us to see the bridges between each process. A precise timeline of the events we observed and discussed is available in Figure 1. We validated these profiles and the processual bracketing during our interviews with the asset manager.

Initial coding: developing first-order codes. We coded our qualitative data to derive our first-order codes. We started by coding our data inductively using open-coding techniques. We then used axial coding to group open-coding codes into categories, going back and forth between our data and the literature. We added "actors" categories (asset manager, asset owners, external committee, portfolio companies) to trace each actor's involvement at each step of the fund's life. We also added "fund life phases" categories (product development, fundraising, investment, monitoring) to link the events and their effects to the identified processes. This thematic, temporal, and actor repartition enabled us to build our results based on a complete processual model recapitulating the events. After coding all our data, we had over 400 open codes across 38 categories. We finally performed a co-occurrence analysis among our codes and categories as we felt that the impact-related codes were related to many other classical codes (conflict & alignment of interests, investment criteria, due diligence, legal negotiations, etc.). This analysis had two main results:

- The impact-related elements are blended in all the other categories. For example, *Impact Strategy* co-occurred with *Investment Strategy* in 84% of its codes,
- Even though we did not witness a complete transaction or monitoring process, our codes relate to all fund's life processes, supporting the results that the creation and fundraising processes affect how the asset manager interacts once the fund is active.

These first two stages resulted in a raw process model describing the key events of a fund's life that will serve as the backbone of our analysis (the black part of Figure 6) and a list of 79 "first-order codes", descriptive and close to informants' terms and perceptions.

Developing the integrated categories and the processual model. At this stage, we tried to make sense of the different identified categories and first-order codes to derive new theoretical

constructs along our processual model. The prior classification of actors and processual bracketings allowed us to deeply understand how early decisions influence the asset manager's subsequent behavior regarding investment and monitoring once the fund is active in the market. This is the stage at which we engaged most with the literature to analyze our data. This interpretative process is reflected in the data structures, where multiple second-order categories are related to one another. For example, we initially focused on identifying the multiple agency relationships that emerged from our case and their potential effect on the actors' behavior. Here, we engaged more deeply with the literature on agency theory and stewardship theory to characterize each actor's behavior and the strategies they used to address agency costs. We thus added to our single *Aligning interests through a persistent governance & control structure* category three other related categories: *Information asymmetry & moral hazard, Signaling ability, Designing incentives and control mechanisms* to better report and understand the organizational mechanisms at play. Similarly, we first approached the fund's impact ambition through the lens of purpose (George et al., 2023) and analyzed it alongside the control mechanisms we observed. We rapidly turned to the literature on hybrid organizations (Battilana et al., 2017) when we realized the actors were coupling practices from the financial and social institutional logics at every level of their organization. This led us to decompose our analysis of the case into two main parts. First, we analyzed the process of fund structuring without considering social impact ambitions to uncover the organizational mechanisms at play, irrespective of extra-financial ambitions. This led us to the *Locking organizational architecture* (Figure 2) and *Framing Effect* (Figure 5) constructs. Then, we analyzed how developing a social impact ambition affected all the dimensions we identified before, developing the *Hybridizing Organizational Architecture* construct (Figure 4). We finally present the results directly using the raw processual model (Figure 6). The resulting integrated model has been presented and validated during our open interviews with the asset manager.

Building external validity. Inductive case studies allow researchers to deeply understand a phenomenon and its underlying mechanisms (Yin, 2009). The main drawback of this methodology is its potential lack of external validity, meaning that our results may not be generalizable beyond the specific case we observed. We thus built this external validity in two ways. First, some of our data relates to the overall private equity industry and not only to our case. The ethnographic author participated in conferences and events gathering private equity professionals to exchange information on the development of sustainable finance, during which he took precise notes on the interventions of industry leaders. The asset owners interviewed also shared insights about their portfolios and offered comparisons with other closely related funds. We also performed two additional interviews with other

asset managers to consolidate our results. Second, previous studies (Bandini et al., 2022; Geczy et al., 2021; Thirion et al., 2022) focused on some isolated elements resulting from our integrated model (e.g. impact-linked carried interest, external committee, pass-through to portfolio companies) and related similar resulting characteristics.

4 Empirical findings

We begin by analyzing the interactions between the asset owners (AOs) and the asset manager (AM)[10] during the fund structuring process. We uncover a locking mechanism through which AOs and AM define the key organizational components of the fund's design (value-creation objectives, resources, control structure) to mitigate agency issues during the active phase of the fund. Second, we analyze how this process evolves to embed the environmental mission in the fund's design, and find that the AOs and AM hybridize the overall organizational architecture of the fund. Finally, we document the effect of the pre-locked architecture on the asset manager's behavior during the active life of the fund and its interactions with (potential) portfolio companies. The results are synthesized in a process model, summarizing the fund's life, in Figure 6, which will be discussed at each step of the analysis, along with supporting quotes from interviews, documents, or ethnographic notes. We provide a complete list of supporting quotes in the Online Appendix.

Figure 6 should go here.

4.1 Locking the organizational architecture to reduce agency costs

Figure 2 should go here.

The first part of our process model (Figure 6) highlights the "structuring" phase of the fund, during which the AM develops the investment policy and raises money from AOs. Because AOs delegate capital but cannot intervene once the fund becomes active, they face agency problems of information asymmetry and moral hazard. To mitigate these tensions, the AM and AOs lock the fund's organizational architecture in advance, so that the AM's actions during the active phase are guided and constrained by the agreed design. This process took 2.5 years and crystallized three interdependent components of the fund: value-creation objectives, resources & capabilities, and the governance & control structures.

[10] In this section, we will refer to the asset manager as AM, and the asset owners as AOs. In Private Equity, investment funds are generally structured as Limited Partnerships. The AM is thus usually referred to as the General Partner, or GP, and the AOs as the Limited Partners, or LPs.

Aligning on investment policy. The investment policy of the fund was first coined by the AM in early 2021 to attract investors. For any fund, it broadly defines how the fund will be invested and managed to get a targeted level of financial returns: targeted assets (e.g., SMEs, start-ups, real assets), financial instruments used (equity-like or debt-like, majority or minority stake), and potentially some specific targeted sectors (e.g., Software, Green Transition, Healthcare). In 2022, it began raising money for the fund (or "pitch") to potential AOs. None of the AOs asked to change the investment policy, they either showed interest and eventually decided to invest in the fund or walked away:

> "During our investment process, we look for funds aligned with our performance and public policy objectives." - *Asset Owner 1*

By this matching process, the AM and the AOs align on the fund's investment policy, which is then locked into contractual terms for the whole fund's life:

> "Investment policy: the Fund is a capital development and buyout fund [...] aiming to build a diversified and balanced portfolio of Investments." - *LP Agreement*

Securing key resources. Second, the AM secured the essential resources it will subsequently use to manage the fund: senior partners with relevant track records, a dedicated investment and impact team, standardized investment and monitoring processes, and external advisors. Concretely, this involved recruiting two senior partners in 2021–2022, designing the composition of the investment team (two investment managers, two associates, and one impact manager with backgrounds in private equity and sustainable finance), acquiring expertise on EU regulations (e.g., EU Taxonomy, SFDR, CSRD) and environmental frameworks (GHG Protocol, SBTi, ACT), and building a network of specialized advisors (legal experts, consultants, M&A advisors for decarbonization and small-cap transactions). These elements were described in marketing documents and presented to AOs during the fundraising process. Although not legally binding, they served as implicit commitments, as overstating resources would harm the AM's reputation and its ability to raise future funds. For example, one marketing document emphasized:

“"Partner 1 and Partner 2 each have 10 years of experience in small-cap private equity, with a proven track record in large industrial groups and the operational management of SMEs." *Private Placement Memoranda - Marketing Document*” The operational backbone of the fund was locked before launch, ensuring the AM would rely on at least these specific resources when executing the strategy.

Configuring governance & control structures. The AM and AOs are subject to both information asymmetry (AOs have limited prior information on the ability of the AM) and moral hazard issues

(AOs cannot engage in the daily management of the fund for legal and operational reasons). We observed multiple strategies used by both actors to mitigate these agency issues. First, they exchanged private information during the pitch process and then during due diligence. In our case, two AOs carried out this due diligence process simultaneously between Q3 2022 and Q1 2023. The AM used it to *signal its ability* by demonstrating that it had secured consistent resources to deliver the strategy (investment team, deal-flow, external advisors, internal processes), thereby reducing information asymmetry. It also signals good faith by designing an initial governance structure that aligns its interests with those of the AOs during the fund's life. They shared private information regarding the AM (history, financials, business plan, ability to raise money and close the fund), the investment team (professional experience, investment track record, personal financial situation, perspectives within the organization), and the fund (in-depth review of the strategy, resources, deal-flow, proposed governance structure). AOs were particularly attentive to the complementarity among the fund's components, including the investment strategy, resources, and proposed governance structure. Second, the AOs and AM engage in legal negotiations to elaborate the contract governing their relationships during the fund's life ("Limited Partnership Agreement" or "LPA" and the "Side Letters" or "SL"). This occurred between Q1 2023 and Q3 2023, subsequently with each AO. They are essential to the AOs, as they cannot engage in the daily management of the fund and thus rely on these to protect their interests for the life of the fund (10-12 years). The resulting LPA synthesizes previous discussion and clearly states the investment policy of the fund, some of the key resources to be used to deliver it (the investment team, the investment process), and the definition of fixed claim rights (over the fund's profits, including the compensation structure of the AM) and fixed control rights (over the fund's assets) between the AM and the AOs. They are tailored depending on the fund's investment strategy and are composed of four main aspects: AM commitment (investing 1% of the total size of the fund with personal money, to get "skin in the game"), AM compensation (2% Management Fees & an incentive up to 20% of the fund's profits as a "Carried Interest"), a set of covenants (sectorial exclusions, diversification ratios, asset types, etc.), and oversight rights for AOs (reporting, creation of an Advisory Committee voting on key issues presenting conflicts of interests, dismissal rights). In line with previous literature (Joseph & Sengul, 2025; Stoelhorst & Vishwanathan, 2024), we distinguish the closely related concepts of governance (the inter-organizational allocation of property rights) from control structure (incentives & control mechanisms), which coordinate behavior within organizational boundaries. Yet, in the case of the independent private equity fund we study, these layers are tightly coupled. The governance negotiated between AOs and the AM directly sets

the parameters of the AM's internal control structure (e.g., hierarchy, decision rights, and incentive systems). Because the same individuals who negotiated the fund's governance subsequently manage it directly, these mechanisms operate simultaneously as an inter-organizational governance structure and an intra-organizational control structure. Moreover, AOs explicitly scrutinized the other elements of the control structure, such as the team's hierarchy and compensation policy, during due diligence as a signal of the AM's credibility and alignment.

> Investment policy: the Fund is a development capital and buyout capital fund, dedicated to environmental transition and decarbonization, in line with the Paris Agreement, which aims to build a diversified and balanced portfolio of Investments [...] It will target companies with an enterprise value generally between €10 and €200 million at the time of the First Investment. [...] The Fund will invest primarily in SMEs through growth and buyout capital transactions to accelerate their organic and external growth [...] - *LP Agreement*

> "The main weapon that enables us to be aligned entirely [between AOs and AM, ndlr] is the legal documents: the LP agreement and the side letter. These are the cornerstones of alignment. They catalyze everything said beforehand [during due diligence and negotiation, ndlr]. Once we have this alignment, the AMs will behave in line with what we want. There's a real job of explaining why we're asking for this, how it will be checked in the future, etc. [...] Of the [multiple dozens] of funds we invest in each year, not all AMs are completely honest. The contract is, therefore, central." - *Asset Owner 1 - Investment Manager*

> "It's the determination of the rules of the game. In fact, we're in the process of writing the book on the rules of the game. Those are the rules that are going to govern the relationship between the AOs and the AM. [...] Obviously, as soon as we start discussing the rules of the game, it's a little complicated because we're not on the same side of the table. So we don't have the same perspective." - *Asset Manager - Managing Partner*

Because the legal contracts are rarely amended, this negotiation process locks the alignment on all the characteristics discussed above: the investment policy (defining the value-creation goals pursued by the fund), the key operational resources (used to pursue the objective), and the governance & control structures (property rights, incentives and control mechanisms used to enforce the pursuit of the stated goals). In this case, the three steps we detailed result in the collaborative locking of the fund's organizational architecture before it begins investing. This locking process occurs during the first five steps of our processual model in Figure 6, i.e., the structuring phase of the fund's life. Following organizational design research (Burton & Obel, 2004; Joseph & Sengul, 2025; Siggelkow, 2011), we define the organizational architecture of the fund as the configuration of (i) the value-creation objectives that guide organizational action, (ii) the resources and capabilities deployed to pursue these objectives, and (iii) the governance & control structures (encompassing the allocation of property rights among key stakeholders and the resulting internal incentives & control mechanisms) that aligns

the AM's behavior with stated goals. From this perspective, the resulting architecture embodies the foundational design choices that establish the organization's internal coherence (Siggelkow, 2002), ultimately shaping how it will operate throughout its lifecycle.

4.2 Hybridizing the organizational architecture to foster social impact

Figure 4 should go here.

We now analyze the evolution of the *Organizational Architecture Locking* triggered by the development of the fund's environmental impact ambition. It led the AM and the AOs to structure the *Organizational Architecture* of the fund by coupling characteristics of from the financial and environmental logics. The investment policy includes financial and environmental goals, the AM developed specific competencies to generate the environmental performance, and the governance & control structure was adjusted to embed the environmental mission. This resulted in actors completely *hybridizing the organizational architecture (objectives, resources, control structure)* of the fund during the structuring process.

> "Typically, in [FUND NAME], it is all over the place [strategy, resources, alignment mechanisms, ndlr] because it's a fund with a detailed and rigorous impact approach. You can't dissociate the investment strategy and ESG components in the case of a fund that aims to decarbonize. It wouldn't make sense. You'd miss the analysis of the investment strategy and policy. We have another fund where the strategy is social impact. If you don't include social impact in your strategy, you've cut something out." - *Asset Owner 2*

Hybridizing the value-creation objectives. In 2021, the AM developed the investment policy by combining objectives from the financial logic (generate financial returns) and the environmental logic (contribute to the environmental transition aligned with the Paris Agreement). Like many hybrid organizations, the fund is subject to legitimacy problems (in our case, potential greenwashing or impactwashing claims) during the structuring phase, particularly concerning environmental logic elements, as its most salient stakeholders (Asset Owners) primarily comply with the financial logic and have limited experience with the other. To mitigate these legitimacy issues and demonstrate the fund's level of commitment to its environmental objectives, the AM built on systemic indicators (GHG emissions) and a science-based reference framework to set the objectives (the Paris Agreement). These systemic referential and indicators were chosen at the inception of the fund's life. They are used to ensure the environmental impact ambition in all the elements of the *Organizational Architecture.*

"Our initial idea has always been to continue to develop the management company through a variety of strategies. And what we've seen over the last few years is a growing desire/pressure from investors to be much more aggressive on CSR and ESG issues. So, we had to solve a twofold equation. First is the financial equation of providing a satisfactory return for investors. If they don't get that return, it's not sustainable [i.e., they would not invest]. Secondly, to be credible in terms of CSR commitment, and to have a methodology that's easy to understand, with a known frame of reference for measurement, and which doesn't open up debates on the interpretation of data and results, the fiddling of subjects, and so on. From that point of view, it had to be relatively irreproachable. So, quite quickly, we came to the subject of decarbonization since, overall, it's the number 1 issue and the absolute priority." - *Asset Manager - Managing Partner*

Moreover, it clearly defined its theory of change and its additionality strategy: it aims to invest both in decarbonizing companies (30% of the assets) and traditional companies to help them decarbonize their activities (70% of the assets).

"We thus thought that we needed to focus on issues related to decarbonization and the Paris Agreements. We need to guide companies that are not making any progress at all and set them on a more virtuous path, or at least one that aligns with the goals of the Paris Agreement. So I'm going to take everyone, and I'm going to help them, I'm going to help them learn how to do it, and I'm going to help them get back to more satisfactory standards [i.e., on the path to alignment to the Paris Agreements]. All in all, this was quite innovative at the time. Ultimately, we weren't wrong since we've seen several competitors emerge with the same strategy." - *Asset Manager - Managing Partner*

The AM combines the goals of the two institutional logics and aims to use the means of the financial logic (shareholder rights and influence on corporate behavior) to achieve the objectives of the environmental logic. This process resulted in a clear definition of an investment strategy that presents multiple value-creation goals and a generic approach to pursue them: contributing to the environmental transition and generating financial returns by investing in SMEs that decarbonize society through their activities or helping traditional companies to decarbonize their operational processes. Through the locking of the organizational architecture, the AOs ultimately aligned on this investment strategy, which was transcribed in the LP Agreement.

"Investment policy: the Fund is a growth and buy-out capital fund dedicated to environmental transition and decarbonization, in line with the Paris Agreement. It aims to build up a diversified and balanced portfolio of investments. [...] It will invest in companies with an enterprise value generally ranging from €10m to €200m at the time of the First Investment. [...] The Fund will invest primarily in SMEs, through growth capital and buyout capital transactions, to accelerate their organic and external growth and their contribution to the decarbonization objectives of the Paris Agreement." - *LP Agreement*

Securing hybrid resources & hybridizing the operational processes. To deliver the dual performance outlined in the fund's investment policy, the AM developed operational processes and secured the key resources required for the fund's active phases in 2021 and 2022. First, the AM recruited the two Partners who manage the fund and supervise the investment team. Both have a hybrid profile, combining experience as private equity investors and in environmental affairs (the energy industry and decarbonizing industrial assets). Then, they designed in Q2 2022 the investment & monitoring processes that would allow them to deliver the financial and environmental performance. For the investment process, they defined a list of investment criteria to analyze the potential of financial & environmental performance: in-house classification based on the activity of the company, willingness of the managers to decarbonize, eligibility for the EU Taxonomy, and identification of potential decarbonization levers. They also defined a set of generic principles to follow when structuring deals, including writing the intention to align with the Paris Agreements into each company's shareholder agreement and designing a compensation package for managers linked to environmental performance. They finally developed a generic monitoring process to improve portfolio companies' environmental performance, including a framework for setting and monitoring science-based GHG emissions targets. These processes blend elements from the financial logic (financial investment criteria, classical deal-structuring tools, shareholder influence on company behavior) and the environmental logic (environmental investment criteria, external systemic referential backing the environmental targets).
Once these processes had been designed, the AM secured the resources necessary to implement them until the end of Q3 2023. As a historically professional private equity organization, it already had the necessary resources and knowledge to pursue the financial objective. We thus focus on developing the resources necessary to achieve the environmental objective. First, the AM completed the team with one investment associate (with private equity experience and training in sustainable finance) and the Impact Manager (a former consultant in environmental transition), whose role is to help portfolio companies decarbonize their activities by implementing the designed monitoring process. Second, the AM deeply studied the local regulations surrounding the environmental transition (e.g., EU Green Deal, EU Taxonomy, SFDR, CSRD, *Loi Energie & Climat, Loi Pacte*) and the main frameworks it could use to back its operational processes and the resulting environmental targets (e.g., SBTi, ACT, EU Taxonomy), to ensure their materiality and back the environmental ambition of the fund. Finally, the AM created an external Impact Committee with independent experts in sustainable finance and the environmental transition (experts from the energy industry, academics, policy-makers, and AOs' representatives) to oversee the environmental part of the operational processes and gathered a

network of potential service providers specializing in environmental transition. Together, these steps outline how the AM hybridized resources and processes to achieve the environmental goals stated in the fund's investment policy.

Hybridizing the governance & control structures. Building on the initial governance and control structures configuration mechanism detailed before, the development of the fund's environmental mission further challenged the alignment between AOs and AM. Developing the fund's environmental mission creates additional agency issues between the AM and the AOs because they are not accustomed to combining components of the two institutional logics. They quickly agreed on the financial components of the governance structure. Still, they had extensive negotiations on the evolution of these components to integrate environmental logic as the indicators & processes used to manage environmental performance were less spread in this industry.

They used multiple strategies to mitigate these additional agency issues during the pitch and legal negotiation processes. Due to increased information asymmetry, the AOs conducted additional due diligence on the operational delivery of the fund's environmental impact strategy (the abovementioned processes and the resources used). The AM used these interactions to *signal* the specific elements it selected from the environmental logic to develop the fund's environmental impact ambition and its operational strategy to deliver it. The AM proved the environmental impact ambition of the fund through compliance with the environmental logic standards (SFDR Article 9 & EU Taxonomy, measuring with the GHG protocol framework, target-setting with SBTi). It then explained in detail the operational strategy (processes and resources) it plans to use to deliver environmental performance. Finally, it signals good faith by proposing an adapted governance structure incorporating the environmental objectives (linking its incentive to impact targets, and creating a new Impact Committee with precise control rights to oversee the activities regarding the environmental process) as an anchor for negotiation of the fund's governance structure.

Developing the fund's environmental objective further complicates moral hazard mitigation since the aim is to ensure that the AM will not only make the necessary efforts to deliver the promised performance but also not favor one objective over the other (e.g., *drifting* toward the sole pursuit of the financial objective during the fund's active phase on the market). To achieve this, the AM and the AOs engaged in extensive negotiations to integrate the environmental objective into the fund's governance structure, thereby aligning their interests throughout the fund's life. They agreed on adapting the control structure through two mechanisms:

- Indexing 20% of the AM's variable compensation (carried interest) to environmental targets

backed by external frameworks (SBTi & Paris Agreements),

- Creating the independent Impact Committee with fixed control rights over the investment process (i.e., analyzing the eligibility of the deals to the fund's environmental objective) and over the target setting & monitoring processes (i.e., validating the environmental targets, the annual reporting, and the final level of achievement once the asset is sold). While this committee only has consultative power, the AM would not take a decision against it due to the reputation risk it would induce, ultimately lowering its ability to raise future funds. Thus, this mechanism is implicitly powerful.

Still, they negotiated particularly on how to set and monitor the environmental targets backing the incentive. While the AM agreed to create an independent Impact Committee and give it fixed control rights on the investment process regarding environmental objectives and the setting & monitoring process of environmental targets at the asset level, it still tried to keep the largest residual control rights possible.

> "No. You have to be really careful what you write and what you say to the LPs during the fundraising process. You mustn't commit to anything too complicated and formal, and keep as much flexibility as possible. [...] You have to try to frame things as much as possible to avoid getting into endless debates. If I were you, what I'd do to keep things simple and effective: send them your notes, but above all, a summary analysis grid to fill in and tick "agree/disagree" at the end. [...] On the other hand, you do something very, very serious about the objectives setting after closing, because that's the most important thing. But in the same way, you have to frame and control as much as possible to have flexibility." *Quote from a Managing Partner - Ethnographic notes*

The AOs were particularly careful to ensure complementarity between the design of these hybrid control mechanisms and the operational processes presented by the AM, to ensure it would lead to the expected environmental impact.

> "[Q: What is the role of legal negotiation and contractual documentation?] For impact funds, we're going to be very demanding when it comes to the LPA, and we're going to make sure that everything is present. In other words, a very clear definition of the strategy, a very clear definition of the impact committee, because generally they have impact committees, and the powers, the corrom, the voting rights, etc. A very clear idea of the incentive mechanism and the formula for determining carried indexation. We therefore ask that this be specified in an appendix or directly in the body of the LPA." - *Asset Owner 2*

> " [...] For [FUND NAME], for example, we have all three: indexation of remuneration, an independent committee, and a methodology backed by proven external benchmarks." - *Asset Owner 1*

Ultimately, developing the fund's environmental ambition led the actors to hybridize all the components of its *Organizational Architecture*: the value creation objectives by integrating the environmental goals into the investment policy, the resources by adapting the financial logic's operational processes to serve the environmental goals and acquiring the new necessary resources, and the governance & control structures by enfranchising the environment using adapted control mechanisms (incentives linked to environmental objectives & oversight through a new committee with fixed control rights).

4.3 The framing effect on the asset manager's behavior

Figure 5 should go here.

The second part of our process model (Figure 6) presents the key steps of the "active" phase of the fund's life, during which the AM invests in and monitors portfolio companies, thereby potentially influencing their behavior. We analyzed these steps on the +60 deal analysis we observed (for which three offers were sent, presenting the financial and legal conditions of the transaction) and one monitoring process. Because these observations occurred while the AM was still fundraising (see the chronology in Figure 1), they enabled us to analyze the influence of interactions with AOs on the AM's investment and monitoring practices as they were occurring closely in time. In particular, the team was actively seeking to close their first deal. It is viewed as a "showcase" of the investment strategy and the quality of the investment team, yielding a clear signal for potential AOs, which could boost fundraising efforts.

> "In fact, the first deals should reflect the investment strategy as closely as possible. [...] It is true that in order for investors to be able to project themselves, they need to visualize the type of deals we want to make. And if these are not aligned with the strategy that has been presented, this will obviously raise questions." - *Asset Manager - Managing Partner*

We document that the behavior of the AM is influenced by the *organizational architecture* of the fund that is locked during the structuring process. Agency and drift may remain possible, but investment decisions unfold within the boundaries materialized by the organizational architecture. This is due to (i) *symmetry of agency settings* that exist between the AOs, the AM, and the managers of the potential portfolio companies, and (ii) the resulting *coherent strategic actions* taken by the AM during the fund's active life.

Symmetry of agency settings. The relationship between the AM and the companies' managers is a classic agency setting (information asymmetry, moral hazard, and hold-up issues) in which the AM is the principal and the managers are the agents. These issues are the same as those facing the AOs and the AM during fundraising, except that the AM was the agent in this previous setting. In particular,

on top of classical financial matters, the environmental objective of the funds also increases agency issues in the relationship between the AM and the managers of portfolio companies, as the AM has no prior information on the environmental awareness and preferences of the managers, and their ability to lead and implement a decarbonization strategy. Thus, the agency settings are symmetrical between the AOs, the AM, and the Management of the potential portfolio companies. Because the AM is an agent in this upward agency relationship, its interests are aligned with those of the AOs through the fund's *organizational architecture locking*. Thus, when aligning its interests with the Management of potential portfolio companies, the AM aligns the interests of the whole investment chain (AOs - AM - Management of portfolio companies). In our specific case, the environmental mission of the fund, being locked in its organizational architecture, cascades down the investment chain in the AM's relationships with managers. A good example of this is the symmetry of the incentive schemes along the investment chain (between AOs and the AM, and between the AM and the managers):

> "As you know, the foundation of our business is alignment of interests. It's really a key cornerstone. [...] The best way to get everyone moving in the same direction is often by aligning economic interests. In any case, that's the choice we made, saying that the whole chain — from the investor down to the manager or executive of the company — has to be incentivized on the same objectives. The best way is indeed to have a management package aligned on both financial and extra-financial objectives. The second level is at the fund: aligning part of the carried interest on both financial and extra-financial objectives. [...] So, in the end, we really have a backbone where everyone shares the same incentives. Everyone looks in the same direction, and everyone rows in the same direction." - *Asset Manager - Managing Partner*

Coherent strategic decisions. The main actions performed by the AM during the active phase of the fund are allocating capital (sourcing, analyzing investment opportunities, structuring deals) and monitoring portfolio companies. Because the AM's interests are aligned with the AOs' interests during the fundraising process through the control structure, all the decisions we observed are consistent with the fund's investment policy. Capital allocation decisions (generating the deal-flow and deciding to invest in companies) heavily depend on the fund's investment strategy. In this case, in the +60 deals observed, the AM systematically used both classic financial criteria (type of deal, management team, company's financials & business plan, strategy & positioning on the market) and environmental criteria (eligibility to the EU Taxonomy, analysis of the carbon footprint & potential for reducing GHG emissions, quantifying potential positive externalities for transition enabling assets). The team discussed in detail these two sets of criteria for each opportunity, leading to debates on the alignment with the investment policy of the funds and ultimately to discarding opportunities.

Note regarding an industrial company (Deal 5): The committee believes in our

environmental thesis but does not believe that we will have a significant impact on the company's behavior. It is true that executives are already aware of the challenges associated with environmental transition and have expressed a need for support on these issues. A key factor for the committee is that the company already has a shareholder fund with an environmental mission similar to ours, and it has had this company in its portfolio for a year. Therefore, even if the company reduces its emissions thanks to the influence and support of its shareholders, we will not be able to take credit for it. "The reality is that we will have virtually no impact on the company, and if it decarbonises, we will mainly say that it is thanks to the managers and [FUND ALREADY SHAREHOLDER], who have been there longer than us. It's also not good for fundraising. It's annoying to be behind them because we won't be able to use this deal to showcase our support." - *Ethnographic notes & Quote from a Managing Partner*

Note regarding an energy services company (Deal 6): On the environmental side, the committee is also challenging. In particular, they refer to a pitch they recently had with an LP, a large mutual insurance group. They were "attacked" on the fact that only 20% of the carried interest was linked to impact objectives, on the pretext that this was not enough to align interests with extra-financial performance. During the committee meeting, one of the partners said: "I ask you this: do you think that with a deal like this you will be able to convince LPs like the ones who [attacked] us over the 20% carried interest? The environmental strategy is not clear here. The impact we're going to have isn't clear either." "To raise funds, we really need the perfect deal in terms of both impact and financial performance, where these LPs will say, 'Oh yes, we didn't understand that." - *Ethnographic notes & Quote from a Managing Partner*

This illustrates how the fund's locked objectives framed the AM's capital allocation decisions, and in this case, making environmental impact potential as central as financial return in investment decisions.

The fund's investment policy also influenced deal structuring and monitoring practices. The AM could only invest in instruments authorized in the LP Agreement (equity-like shares) and systematically designed control mechanisms to align the interests of portfolio managers with those of the fund and to secure the necessary rights for effective monitoring. For all the companies we met, the AM explicitly presented both the fund's environmental mission and the resources available to support decarbonization, to test whether these ambitions matched the willingness and expectations of the target firms' managers. This ensured that environmental considerations were integrated from the very first interactions. For the three cases where offers were sent, the AM detailed the control structure it proposed to shareholders and managers: a management package indexed to the achievement of environmental targets, a clause in the shareholder agreement explicitly aligning the company with the Paris Agreement, including a survival clause in case of exit, a board seat, and a precise description of the support process and the resources mobilized by the AM to help the company reach its objectives. These

proposed terms illustrate how deal structuring was already embedding environmental performance within the same legal and incentive mechanisms traditionally used for financial alignment.

> "We finished negotiating the fund mandate with our key investors, and you participated in some investment processes for which we sent letters of interest, even though they did not go through in the end. Yes, it would be better if you'd seen a proper deal going through and the monitoring process, but we would just apply everything we agreed on with our investors." - *Asset Manager - Managing Partner*
> "Everything in the contracts [at the fund level, NDLR] has a clear impact on the life of the fund and their [the AM, ndlr] decisions regarding the fund's management." - *Asset Owner 1 - Investment Manager*

We thus document that the fund's organizational architecture has a *framing effect* on the AM's behavior with (potential) portfolio companies. It is essential to note that this framing occurs through the organizational components at the fund level, particularly the governance & control structures (including compensation and oversight rights), which enforce the previous alignment of the AOs and the AM on the investment strategy and the resources allocated to pursue it. This is also in line with Geczy et al. (2021)' finding that funds with operational impact commitments in their contracts tend to enforce strict impact terms in their contracts with portfolio companies, or Edmans et al. (2024) reporting that 71% of investment managers take sustainable investment action (stock selection, engagement, voting) due to constraints in their mandates or firm-wide policies.

5 Discussion

In this study, we open the black box of investment organizations to explain how their organizational architecture is designed and how it shapes investors' behavior in capital markets and, ultimately, their social impact. Building on an in-depth case study of a private equity impact fund, we identify three organizational mechanisms (locking, hybridizing, and the framing effect) that jointly explain how asset managers and asset owners build investment organizations' architecture and their effects on subsequent behavior. Integrating our findings with research on sustainable finance (Kölbel et al., 2020; Marti et al., 2024) and organizational design (Joseph & Sengul, 2025), we propose a process model (7) that describes this structuring process and its evolution to foster social impact. While prior research has emphasized capital allocation and shareholder engagement as the primary levers through which investors influence companies, we show that these levers are shaped by the organizational architecture defined by early interactions between asset managers and their beneficiaries. We provide a simple integrative framework to capture these architectures by conceptualizing them as systems of

interdependent components (value-creation objectives, resources & capabilities, and control & governance structures) whose coherence and complementarity determine the degree of the investment organizations' internal fit.

Figure 7 should go here.

This perspective contributes to corporate governance by revealing the organizational foundations of agency capitalism and to sustainable finance by framing it as an organizational design problem.

5.1 The organizational foundations of agency capitalism

We contribute to the growing literature on the effects of intermediation in our financial system by studying it as an organizational phenomenon. Prior research have largely examined the legal (Fisch, 2010; Gilson & Gordon, 2013) and economic (Bebchuk et al., 2017; Heath et al., 2021; Lewellen & Lewellen, 2022) features of investment mandates, concluding that this new form of *agency capitalism* further decouples ownership and control of firms and leads to an undervaluation of governance rights, especially for passive mutual funds such as index funds (Heath et al., 2021).

In this paper, we move beyond economic considerations and extend the concept of *agency capitalism* to its organizational foundations by studying how investment organizations (such mutual funds, hedge funds, or other types of institutional investors) are structured during the interactions between asset managers and their beneficiaries, and documenting the framing effect it has on their subsequent behavior. We uncover that to mitigate agency costs (Jensen & Meckling, 1976), asset managers and their beneficiaries stabilize (implicitly through commercial commitments or explicitly through contractual agreements) multiple key interdependent components of the architecture (Jensen & Heckling, 1995; Siggelkow, 2011) of investment organizations, such as value-creation objectives, resources, and the governance & control structures, before they operate on the financial markets. As for any organization, the design of investment organizations (Donaldson, 2001; Donaldson & Joffe, 2014) has important implications for subsequent information processing, decision-making, coordination, and ultimately performance. We provide qualitative evidence that the governance mechanisms observed in shareholder–company interactions (Edmans & Holderness, 2017) are mainly shaped by upstream relationships between institutional investors and their beneficiaries, as reflected in the resulting architectures of investment organizations. Doing so, we argue that institutional investors' behavior is indeed driven by the design of their mandates, not solely through contractual incentives (Bebchuk et al., 2017; Lewellen & Lewellen, 2022), but by the organizational architecture co-defined with their beneficiaries, bringing the organizational dimension of agency costs of agency capitalism. While our

analysis focuses on the last layer of intermediation between asset owners and asset managers, investment chains often involve multiple nested layers of delegation (Arjalies et al., 2017). Each link in this chain reproduces (and can amplify) the organizational mechanisms we identify, further constraining managerial discretion and reinforcing the locking process across levels.

This has several implications for corporate governance studies and, in particular, for the current debates regarding shareholder supremacy (Battilana et al., 2022; Freeman et al., 2004; Goranova & Ryan, 2022; Jensen, 2001), and corporate purpose (George et al., 2023; Mayer, 2021; McGahan, 2021; Segrestin et al., 2021). First, our results support the argument that the concept of homogeneous shareholders maximizing financial value is outdated (Fisch, 2010; Gilson & Gordon, 2013; Goranova & Ryan, 2022), as institutional investors' interests can vary based on the value-creation objectives they defined with their beneficiaries. Time horizon (DesJardine et al., 2022), for instance, becomes an important parameter of these objectives. In this context, scholars could use organization and governance theories (Joseph & Sengul, 2025) to analyze investors' architectures and systematically capture their heterogeneity. As agency issues are salient for investment organizations (Bebchuk et al., 2017), control (Cardinal et al., 2017; Eisenhardt, 1985) and configuration (Miller, 1996) streams seem particularly relevant to map these architectures, define the heterogeneous interests of shareholders, and better understand the determinants of their actions on the market. Recognizing investors as organizations provides an avenue to enrich corporate governance theory by shifting the focus from shareholder incentives to the organizational architectures that underpin their behavior.

Second, shareholder supremacy has been a long-standing debate in the corporate governance literature (Battilana et al., 2022; Bridoux & Stoelhorst, 2022; Freeman & Reed, 1983; Freeman et al., 2004; Jensen, 2001; Stoelhorst & Vishwanathan, 2024), with recent studies arguing firms' purpose should include a social dimension (Chua et al., 2024; George et al., 2023; Mayer, 2021; Segrestin et al., 2021). This stream of work usually considers shareholders as atomistic, financial-value-maximizing agents, potentially compromising firms' sustainability by extracting value from other key stakeholders. Our results suggest a more nuanced understanding of shareholder behavior. In line with Hart and Zingales (2022), we posit that the role of firms is to maximize shareholder *welfare*, which has indeed historically been translated into financial value in theory and practice. According to our results, most shareholders are investment organizations (Aguilera et al., 2025; Bebchuk & Hirst, 2019) that vary in their interests (or definition of *welfare*) and actions due to their different organizational architectures. Like any organization, they could be reformed to enfranchise key stakeholders (McGahan, 2023a; Stoelhorst & Vishwanathan, 2024) and to take into account their interests when investing & monitoring companies,

ultimately serving as a vector of purpose (George et al., 2023) and social impact. As shareholders remain the most salient stakeholders for firms under the current design of market institutions, it might be more effective to let traditional market mechanisms continue to govern firm–shareholder relationships, while ensuring that shareholders themselves integrate key sustainability concerns (e.g., environmental protection) directly into their organizational architectures. By embedding stakeholder interests in the design of investment organizations, these reformed shareholders would transmit broader social preferences into market mechanisms (Yan et al., 2021). Because asset prices aggregate the beliefs and preferences of investors, the upstream enfranchisement of stakeholders would be reflected in price signals, capital allocation, and monitoring decisions. In this view, financial markets could retain their allocative efficiency (continuing to channel capital toward its most valued uses) while incorporating a richer definition of value that internalizes the interests of a broader set of stakeholders. Rather than replacing market coordination with political or regulatory control, this approach redefines the organizations that participate in the market. Building on this insight, the next section analyzes how incorporating social objectives into investors' architectures transforms them into hybrid organizations and creates new design challenges, central to sustainable finance.

5.2 Sustainable finance as an organizational puzzle

Second, we contribute to the literature on sustainable finance by establishing the organizational foundations of this phenomenon and uncovering the crucial role of interactions between asset owners and asset managers in shaping the social impact potential of investment practices. Existing research has explained how investors can influence companies in financial markets (Broccardo et al., 2022; Kölbel et al., 2020) through capital allocation (Heinkel et al., 2001; Oehmke & Opp, 2025; Pástor et al., 2021) and engagement (Barko et al., 2021; Dimson et al., 2015; Flammer et al., 2021) practices, and whether they can yield a positive social impact. Yet this stream has overlooked the intermediated character of our financial system, even in management and organization studies (Chuah et al., 2024; DesJardine et al., 2024; Ferraro & Beunza, 2018; Marti et al., 2024; Slager et al., 2023). Recent evidence, however, suggests that asset managers' social and environmental actions are primarily driven by their mandates (Edmans et al., 2024). Building on this insight, we uncover the organizational mechanisms that explain why: the negotiation between asset owners and asset managers acts as an organizational design driver for investment organizations, potentially embedding both social and financial objectives into their very structure. Integrating social objectives into the value-creation objectives of investment organizations makes them gradually hybrid (Battilana et al., 2017; Greenwood

et al., 2011), with goals that are ambiguously or weakly correlated (Ethiraj & Levinthal, 2009), thereby amplifying the traditional agency issues between asset owners and asset managers and creating internal coordination tensions. As for any hybrid organization (Battilana, 2018; Battilana & Dorado, 2010), these new tensions can be managed by adapting each component of the design (value-creation objectives, resources, control structure) of the investment organization to properly *lock* its social mission and subsequently *frame* consistent capital allocation & shareholder engagement practices. We thus theorize sustainable finance as an organizational design problem (Burton & Obel, 2004, 2018; Siggelkow, 2011) under conditions of hybridity (Battilana et al., 2017), which is handled through interactions between asset managers and their beneficiaries. Grounding sustainable finance as an organizational design problem provides a foundation to bridge previously isolated insights regarding the varying social ambitions & strategies of investors (Busch et al., 2021), their contracting (Geczy et al., 2021; Thirion et al., 2022), reporting (Kaufmann et al., 2025), and business models structuring (Bandini et al., 2022) practices.

We first interpret the heterogeneity in investors' social ambitions as a variation of the degree of hybridization of their value-creation objectives. Building on Busch et al. (2021)'s classification of sustainable finance strategies, we conceptualize differences in stated social ambitions (from minimal ESG risk integration to impact-first mandates) as a continuum of hybridization of investment organizations' goals. At one end, investors primarily guided by financial logic incorporate social criteria instrumentally, as risk mitigants, at the other, impact-first investors embed social outcomes as coequal ends. Between these extremes lie multiple intermediate forms, each reflecting a distinct configuration between the social and financial logics (Besharov & Smith, 2014), and corresponding to a distinct level of organizational complexity (Greenwood et al., 2011). The centrality of the social mission and the associated organizational complexity depend on their strategy for delivering social impact (or "Theory of Change") and the resulting compatibility between logics (Yan et al., 2021). For example, investors primarily using the capital allocation mechanism to fund impact-native projects (such as impact investors funding social enterprises, blended finance organizations, or stock-picking SRI funds) will face a different type of complexity than those using the engagement mechanism to influence corporate behavior, as the latter is generally more costly and the relation between social and financial outcomes in this case is more blurry (Ethiraj & Levinthal, 2009). Thus, we conceptualize investors' social ambitions as an organizational design choice that determines the degree of hybridity in their objectives, which further requires aligning the resource system and the governance & control structure.

Second, the pursuit of multiple objectives requires adaptation of the organization's resources & capabilities (Battilana, 2018; Battilana & Dorado, 2010). Consistent with Bandini et al. (2022), we document that investors selectively couple (Pache & Santos, 2013) their resources (encompassing team members, network of partners, operational processes) from the social and financial logics to deliver the dual performance and maintain legitimacy toward their stakeholders.

The governance & control structures are the third key component of this design framework, translating objectives and resources into coordinated actions. At the governance level, investment organizations can enfranchise stakeholders toward whom they aim to create value (McGahan, 2023a) by allocating specific property rights to them (Alchian & Demsetz, 1973; Klein et al., 2019; Stoelhorst & Vishwanathan, 2024). In our case, the fund's social mission is embedded in its governance structure by granting the environment (represented by a dedicated impact committee) fixed control rights over investment and monitoring decisions, and residual claim rights through the asset manager's impact-linked incentive scheme. These arrangements perform a dual function. Contractually, they align incentives between asset owners and managers, as documented in prior research on impact investing (Geczy et al., 2021; Thirion et al., 2022). From an organizational perspective, they *lock* the social mission into the fund's architecture by assigning enduring rights to the stakeholder it seeks to benefit. This structure then filters competing institutional pressures (Battilana et al., 2022), sustains hybridity over time, and protects against mission drift (Ebrahim et al., 2014; Mair et al., 2015), notably by creating spaces of negotiations (Battilana et al., 2015) to arbitrate between the expectations of multiple stakeholders. Such a governance structure remains external, mediating the relationship between the investment organization and its broader stakeholder ecosystem, and can cascade internally into control systems and routines that translate this social mission into day-to-day behavior. Following previous organizational literature, we define the internal control structure as a set of incentives (Gibbons, 2005) and control mechanisms (Cardinal et al., 2004) used to align the behavior of members (who can have different skills, preferences, and goals) toward the organizational objectives and mitigate the internal agency problems (Fama, 1980). In the case studied, it takes the form of the carried interest linked to impact-performance and the whole control system (systematic reporting backed by scientific referential, impact committee overseeing the activities) designed around the social mission.[11] Control systems channel members' attention (Ocasio, 1997; Ocasio & Wohlgezogen, 2010) toward intermediate

[11] In our case, the governance–control nexus is particularly tight: because the fund and the asset-management team largely overlap, the incentives and control mechanisms defined between the asset manager and its beneficiaries cascade directly to individuals operating the fund. Nevertheless, we conceptualize governance as the external component (locking the social mission through an allocation of property rights) of the design and control as the internal component (translating that social mission into routines, metrics, and behaviors). Together, they embody the locking of investment organizations' design: governance locks the social mission externally, and control enacts it internally.

objectives (Simon, 1957), providing them with frames through which to interpret information about their environment (S. Kaplan, 2011) and routines that guide actions (S. Kaplan & Henderson, 2005). This channelization is critical in such hybrid organizations, as it frames the potential arbitrages between multiple logics (Battilana, 2018) and allocates the attention of decision makers to the relevant stakeholders (Crilly & Sloan, 2014; Pache et al., 2024). In impact investing, for example, Kaufmann et al. (2025) reports that impact measurement and reporting systems primarily serve relational and interpretive functions rather than accountability or performance management. Taken together, the governance and control structures of investment organizations formalize the guardrails of each logic (Smith & Besharov, 2019), enabling investment team members to navigate conflicting demands of the financial and social logic while maintaining agency and legitimacy.

Finally, this integrative perspective highlights that these components are interdependent and must be examined jointly rather than in isolation: the effectiveness of one depends on its alignment with the others. Grounded in organizational design theory (Burton & Obel, 2004, 2018; Joseph & Sengul, 2025; Siggelkow, 2011) and informed by research on hybrid organizations (Battilana, 2018; Smith & Besharov, 2019), we emphasize that the internal fit of investment organizations depends on the coherence and complementarity among these components rather than on the sophistication of any single mechanism. Such systemic alignment determines whether they can sustain dual performance over time and ultimately deliver social impact.

5.3 Managerial & Policy Implications

Our findings carry important implications for how investment professionals and policymakers conceive and evaluate sustainable finance practices. We show that the social impact potential of sustainable finance is largely built upstream during the interactions between asset owners and asset managers when investment mandates are negotiated and funds are structured. These interactions are moments of organizational design, in which the fund's objectives, resources, and governance systems are defined. The way these components are assembled conditions the organization's subsequent behavior in financial markets and its ability to pursue multiple objectives. Asset owners and regulators should therefore recognize that these design features are the organizational antecedents of investors' behavior and impact performance.

Analyzing investment organizations through this lens requires focusing on their internal architecture as a coherent, complementary system rather than as a set of isolated mechanisms. Evaluating objectives, resource configurations, and governance or control systems separately offers only a partial

view of their functioning. It is the coherence and complementarity among these components that matter to sustain a balance between financial and social performance. For practitioners, this means that fine-tuning individual mechanisms (such as fee structures or incentive schemes) without aligning them with other design components risks creating inconsistencies that erode the organization's mission over time.

This organizational perspective finally calls for an evolution of reporting and regulatory frameworks. Current initiatives adopt different approaches to assessing responsible investment practices, but most remain misaligned with the organizational level at which impact is built. For example, the EU Sustainable Finance Disclosure Regulation (SFDR) operates at the fund level, which is appropriate, yet focuses primarily on ex post portfolio outcomes rather than on the ex ante organizational features that condition them. In contrast, the UN Principles for Responsible Investment (PRI) collect disclosures at the asset manager level, overlooking the heterogeneity of the investment vehicles they host. Because asset managers often manage multiple, sometimes conflicting mandates, the relevant analytical unit for evaluating social impact is the investment vehicle itself, which is governed by a specific organizational architecture and mandate. Reporting systems should therefore complement outcome-based metrics with disclosures on the architectural features of investment vehicles, as they may provide more reliable indicators of a fund's capacity to deliver social impact.

5.4 Limitations & Future Research

This study has several limitations. First, even if they resonate with recent evidence (Bandini et al., 2022; Geczy et al., 2021; Kaufmann et al., 2025; Thirion et al., 2022), our findings rely on a single case, which constrains their external validity. Second, the private equity context may appear specific, as it involves high agency costs and intermediation by multiple layers of professional organizations. Yet, these characteristics do not constitute strict boundary conditions: the mechanisms identified arise from financial intermediation itself, which is a common feature across asset classes. Future studies could therefore test and extend our framework in other settings such as listed equity or fixed income, or higher in the investment chain, where the power balance between asset owners and asset managers and the resulting agency issues may differ.

Future research could also investigate how variations in organizational design translate into differences in market behavior and performance. Large-sample or comparative studies could examine whether funds displaying higher internal coherence and hybridization also exhibit more consistent capital allocation or engagement strategies, and potentially superior social outcomes. Exploring mul-

tiple levels of intermediation would also provide a deeper understanding of systemic alignment on social issues in our financial system.

In particular, a promising avenue is to explore the meta-organizational nature of investment organizations. Investment funds are typically housed within larger asset management firms or financial institutions, whose governance structures, culture, and incentive systems may influence the specific mandates they host. These nested forms of governance create multi-level interdependencies that can either reinforce or undermine the alignment achieved at the fund level. Understanding how these cross-level dynamics operate would advance the study of hybrid organizing and offer a more complete account of how financial institutions internalize social purposes. In our case, the asset management company progressively extended its environmental engagement practices to other mandates, suggesting that successful hybridization at one level can diffuse throughout the organization.

More broadly, our results invite scholars to reconsider the financial system itself as a network of organizations whose design determines the extent to which they can serve social goals. Rather than focusing on reforms of market institutions or corporate law that constrain shareholder rights, future research could examine how and to what extent stakeholders can be enfranchised within the governance of financial institutions, and how such enfranchisement may diffuse internally across organizational layers, across intermediation layers within the financial system, and to corporate practices through market mechanisms. Such an inquiry would illuminate the organizational channels through which financial institutions transmit social preferences from ultimate owners to companies and potentially reconcile market allocation efficiency with social responsibility. To synthesize, recognizing investors as organizations fundamentally alters the analytical lens through which corporate governance and sustainable finance practices are studied. We identified some research opportunities in this paper, but we believe integrating organizational theory into the study of sustainable finance represents a larger momentous research agenda.

6 Conclusion

In this study, we opened the black box of investment organizations by examining how their asset owners and asset managers jointly design them to pursue financial and social objectives. Drawing on a case-study of a private equity impact fund, we identified three interrelated mechanisms that explain how intermediation shapes institutional investors' behavior and, with it, the social impact potential of sustainable finance. Together, these mechanisms reveal that the social impact potential of an investment organization depends on the coherence of its internal architecture, locked ex ante.

Achieving such internal fit (Burton & Obel, 2018) requires a comprehensive hybridization of objectives, resources, and control structures, a process through which financial and social logics become mutually reinforcing rather than competing. While previous work has examined how investors influence firms through allocation or engagement mechanisms, we show that these downstream actions are conditioned by upstream design choices negotiated between asset owners and asset managers. Understanding this structuring process is essential to unlock the social impact potential of sustainable finance. By making explicit the organizational mechanisms shaping this structuring phase, our study offers a first step toward a grounded theory of how investors' architectures determine their market behavior and impact, and build the organizational foundations of agency capitalism and sustainable finance.

In conclusion, reframing sustainable finance as an organizational design issue shifts the central question from what markets can do for society to how the organizations that enact market mechanisms are themselves designed to serve society. By tracing how institutional investors' organizational architectures emerge and shape their behavior, we offer a foundation for analyzing social impact potential of finance. Building on this foundation will require both scholarly and practical efforts to rethink the structures through which capital is mobilized, governed, and ultimately made accountable to society.

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A Data summary

Meeting type	Length (hours)
Investment	81:50:00
Monitoring	2:30:00
Fundraising & Structuring	16:15:00
Industry Events & Working groups	26:20:00
Regular interviews with investment team	8:30:00
Total	**135:25:00**

Table 1: Participant Observation - Summary of observed meetings

These statistics only include formal meetings logged in the ethnographic author's calendar. He also participated in and took notes on the preparation and debriefings of these formal meetings, and in many other informal meetings.

Name	Date	Length	Description
Asset Owner 1	08/2023	60min	First investor of the fund. Public Investor. Investment Team Manager.
Asset Owner 2	08/2023	120min	Second investor of the fund. Public investor. Investment Team Member.
Asset Owner 2	09/2024	50min	Second investor of the fund. Public investor. Head of Fund of Fund activities.
Asset Manager - Regular interviews	1/1.5month	n.a.	Feedback interviews with the investment team partners.
Asset Manager - Managing partner 1	06/2020	70min	C-Level of the fund management company.
Asset Manager - Managing Partner 2	06/2024	90min	C-Level of the fund management company.

Table 2: Interviews - Summary

Documents	Process	Actors	Length
Investment Memos & Offer Letters	Investment	AM,PCs	203p
Marketing (PPM, etc.) & Contractual documents (LPA, SLs)	Fund structuring	AM, AOs	483p
Audit reports & Monitoring Memos	Monitoring	AM,PCs	22p
Total			**718p**

Table 3: Interviews - Summary

B Tables & Figures

Strategy	Environmental Impact Buy-out Fund
Expected Size	€[100-150]m
Deal type	LBO, Transmission, Development
Targets profile	SMEs, Profitable / Mature
Investment tickets	€[5-15]m
Market Segment	Small Cap (Enterprise Value < €150m generally)
Financial Return Target	Market-standard [20-25% IRR, 2.5x-3x MoIC]
Impact strategy	Environmental transition, GHG emissions reduction in line with the Paris Agreement. Achieved by investing in standard SMEs and helping them to decarbonize their activities (80% of the expected portfolio) or in SMEs whose activities help decarbonize the economy (e.g., cleantech companies, 20% of the expected portfolio).
Impact measurement & referential	CO_2 emissions, alignment to Paris Agreement
Fees & Carried Interest	2% Management Fees, 20% Carried Interest, 20% of the carried interest is linked to impact objectives.
Governance	Investment Committee, Impact Committee, Advisory Committee
SFDR	Article 9

Table 4: Summary of the main characteristics of the fund studied

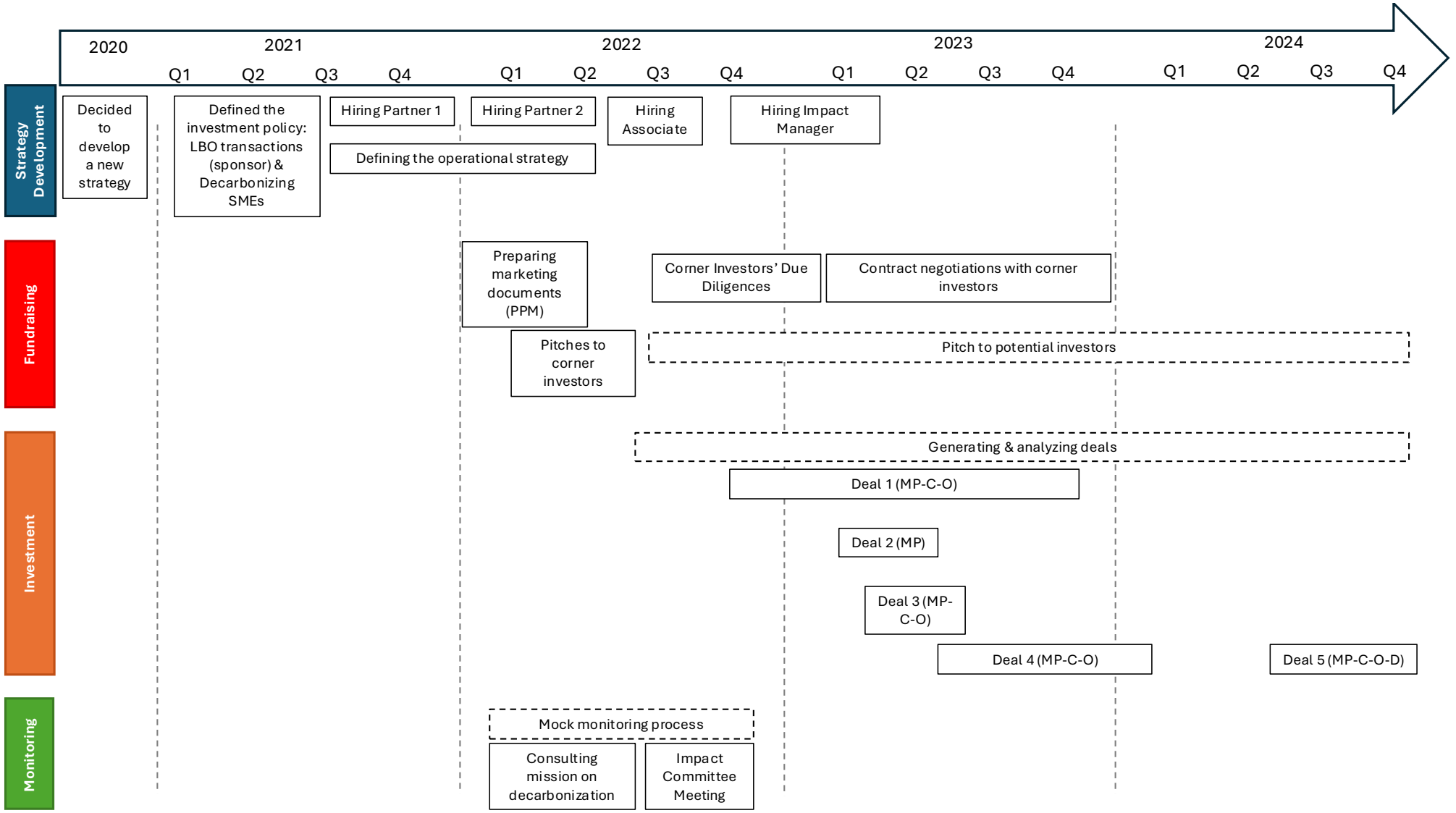

Figure 1: Timeline of events (2020-2024)

Note: This timeline chronologically presents the main events we observed and classified with our decomposition of a fund's lifecycle. For investment:

- MP = "Management Presentation", i.e., the investment team met with the management team of the target company,
- C = "Investment Committee", i.e., the investment team drafted an investment memo and presented it to the Investment Committee of the fund,
- O = "Offer", i.e., the investment team sent an offer letter to the target company.

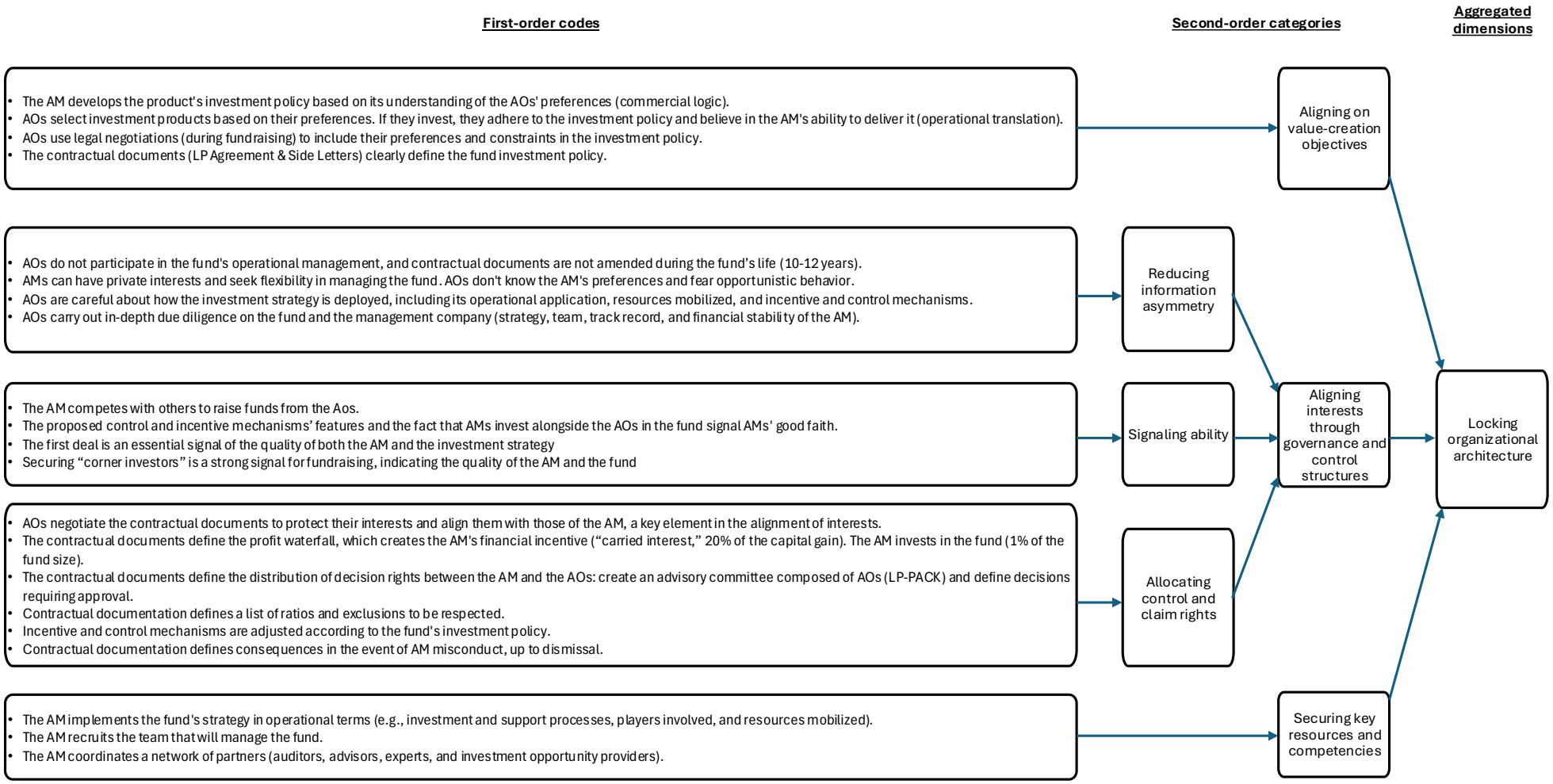

Figure 2: Data Structure - Locking organizational architecture

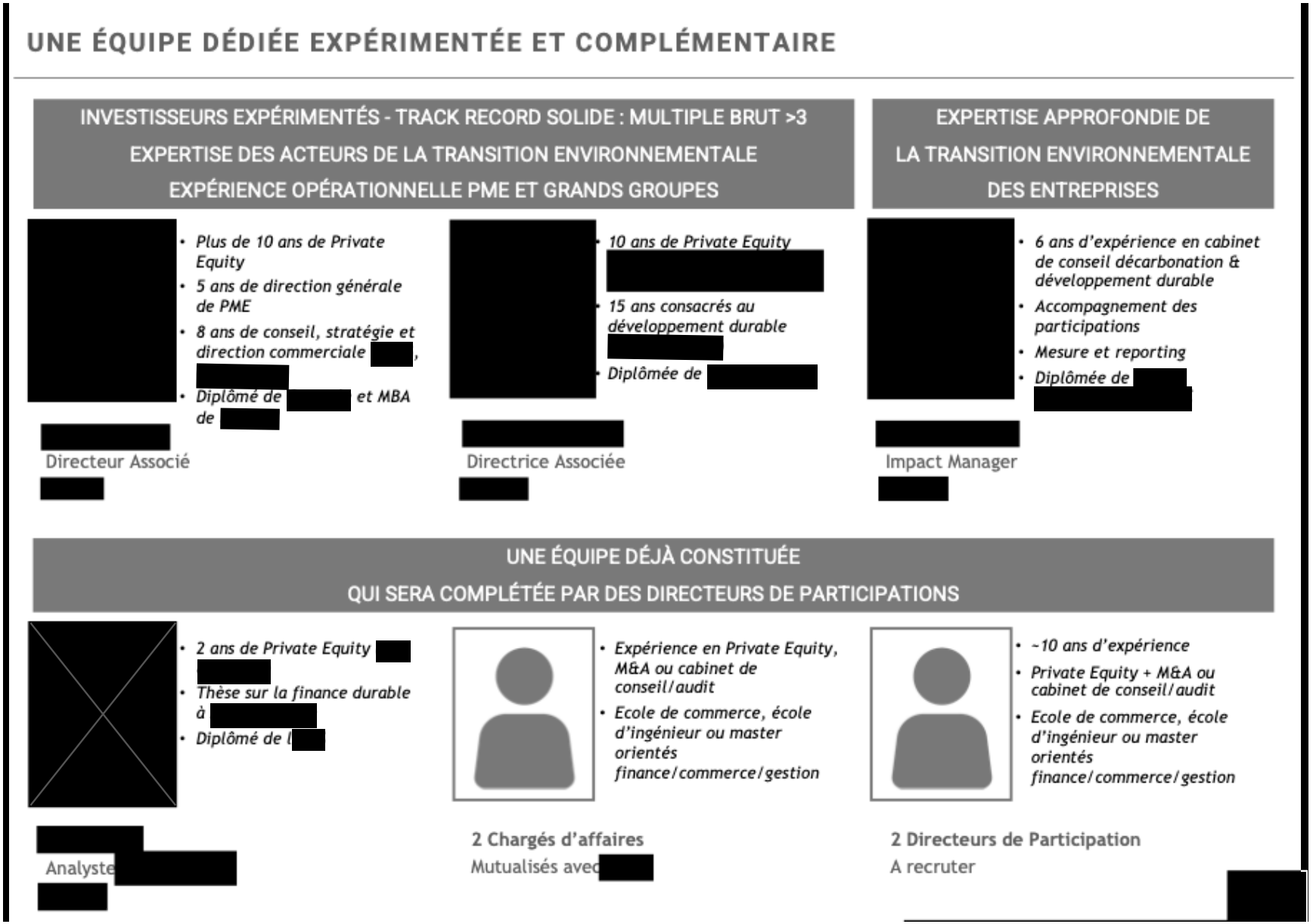

Figure 3: Team Members Overview (Extract from the marketing prospectus)

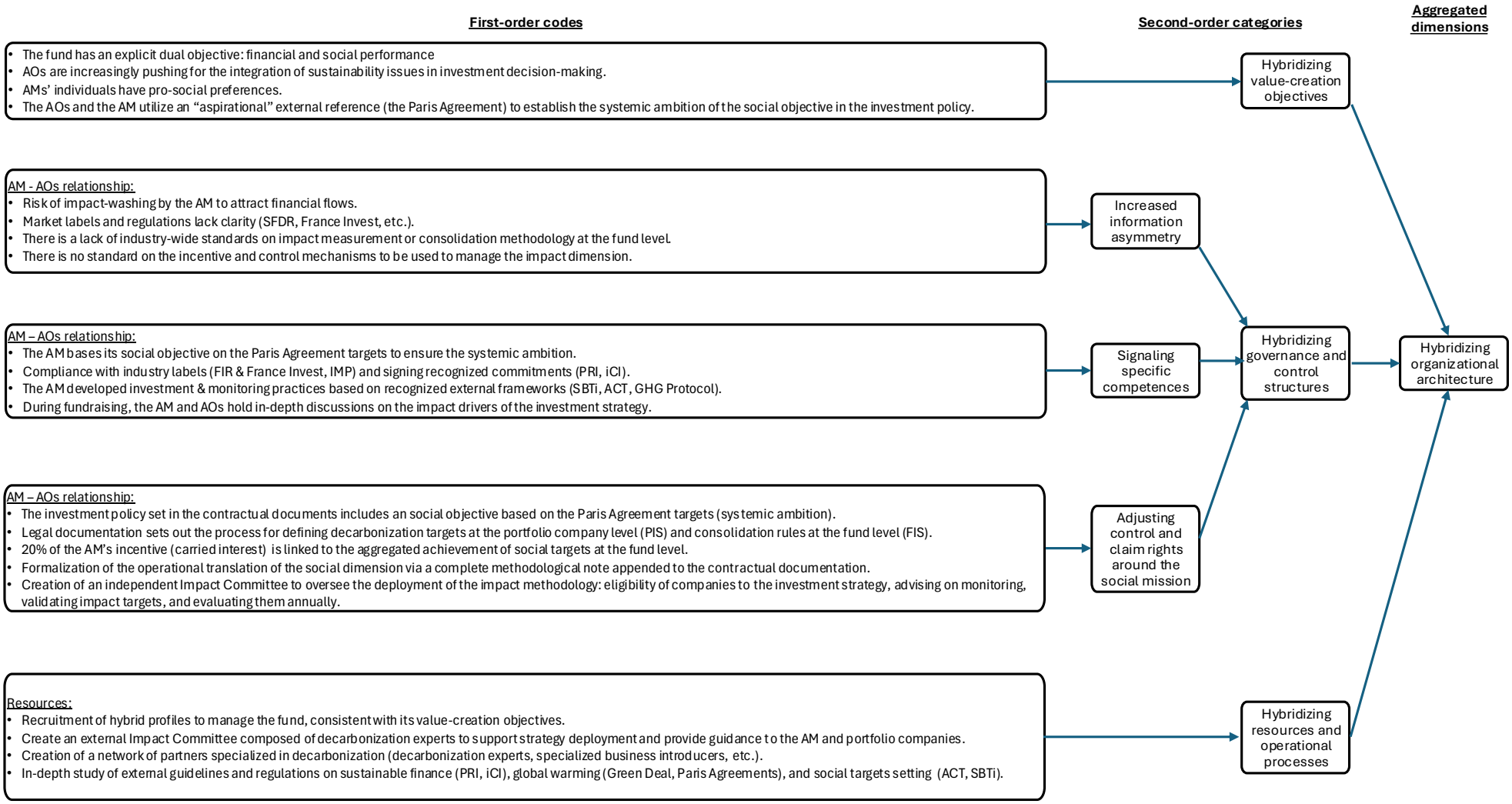

Figure 4: Data Structure: Hybridizing organizational architecture

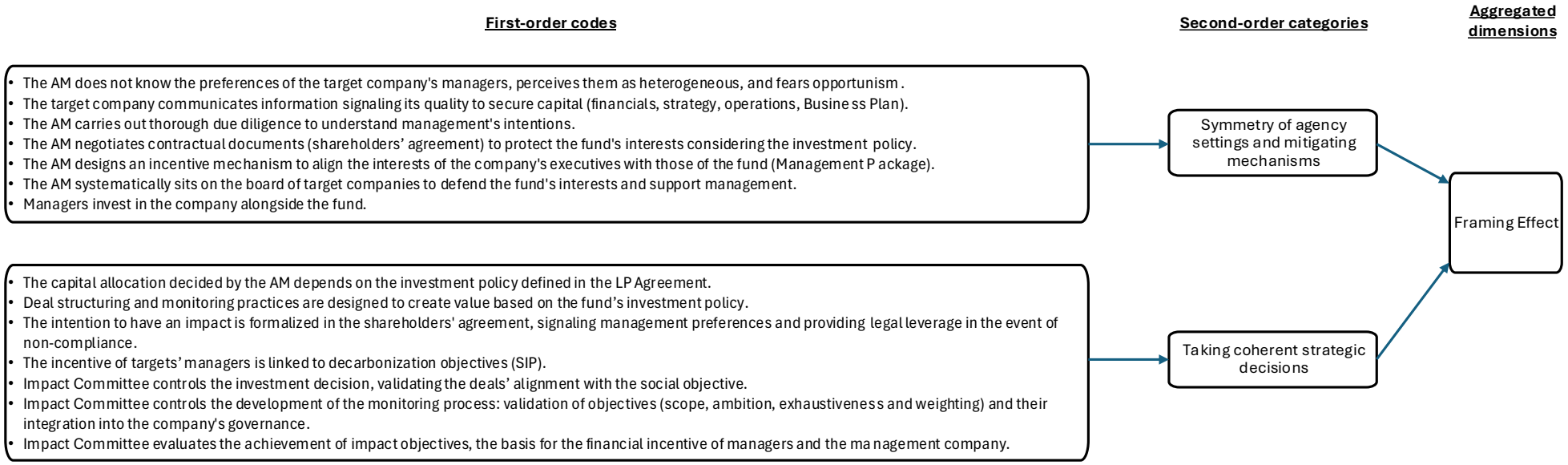

Figure 5: Data Structure: Framing Effect

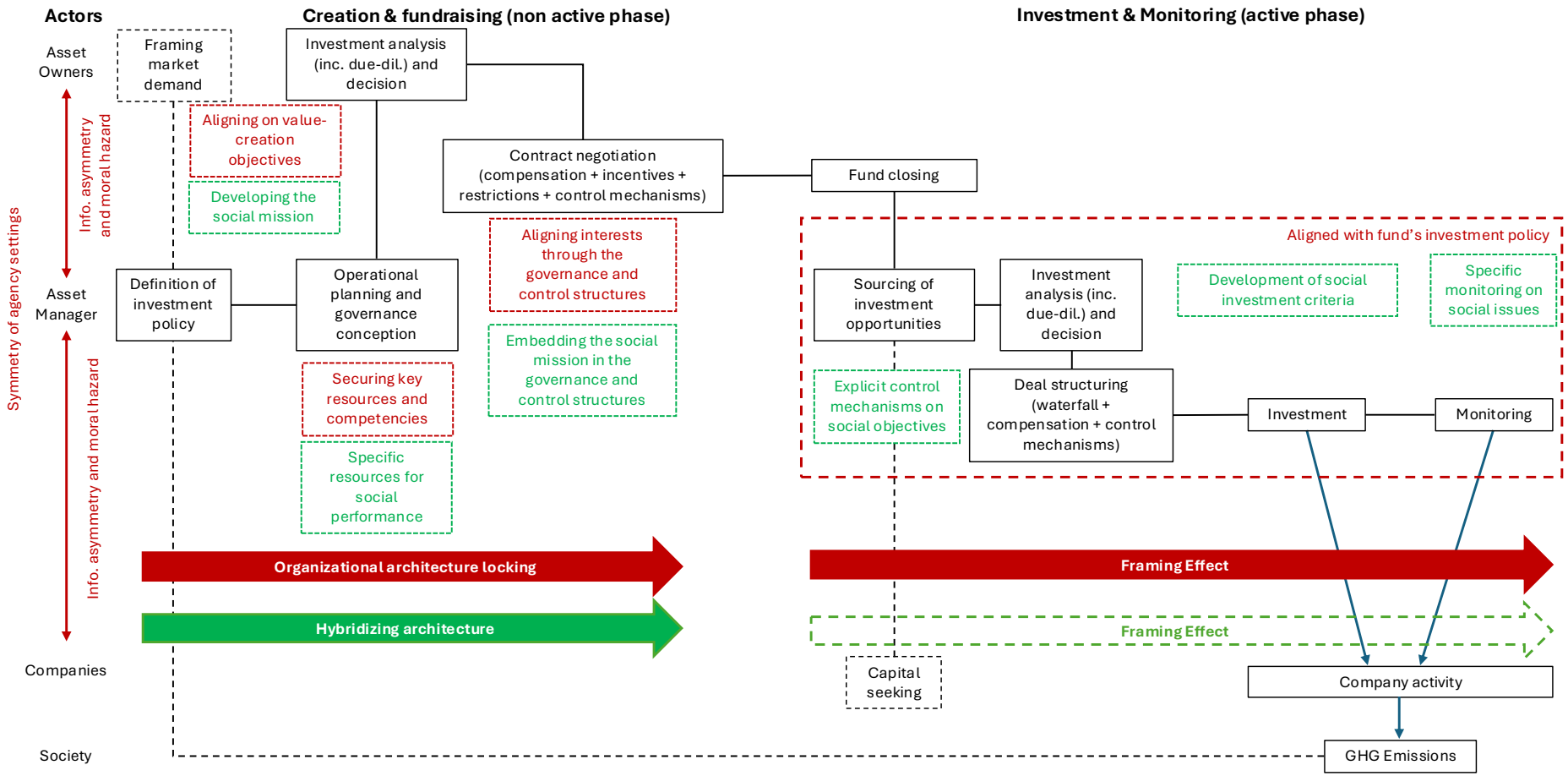

Figure 6: Complete processual model - Hybridizing investment organizations

Note: This model presents our findings along the fund's lifecycle, drawn as a standard business process model. The participating players are listed on the left side (Asset Owners, Asset Manager, Companies, Society), and we split the fund's lifecycle into two main phases (Creation & Fundraising and Investment & Monitoring). The black part of the model represents the raw observed events and is horizontally aligned with the actors involved (e.g., "Definition of the investment policy" involves only the Asset Manager). Each black line represents a new chronological step, with dotted lines representing indirect effects influencing the events. The red & green elements represent our analysis and results (second-order themes in squares and the aggregate dimensions in arrows). With this model, we see for example that Asset Owners have a significant influence during the fund's structuring process (aligning on the investment policy, aligning interests) before the fund is closed and starts to invest, and do not interact with the fund or the asset manager during the investment and monitoring phase.

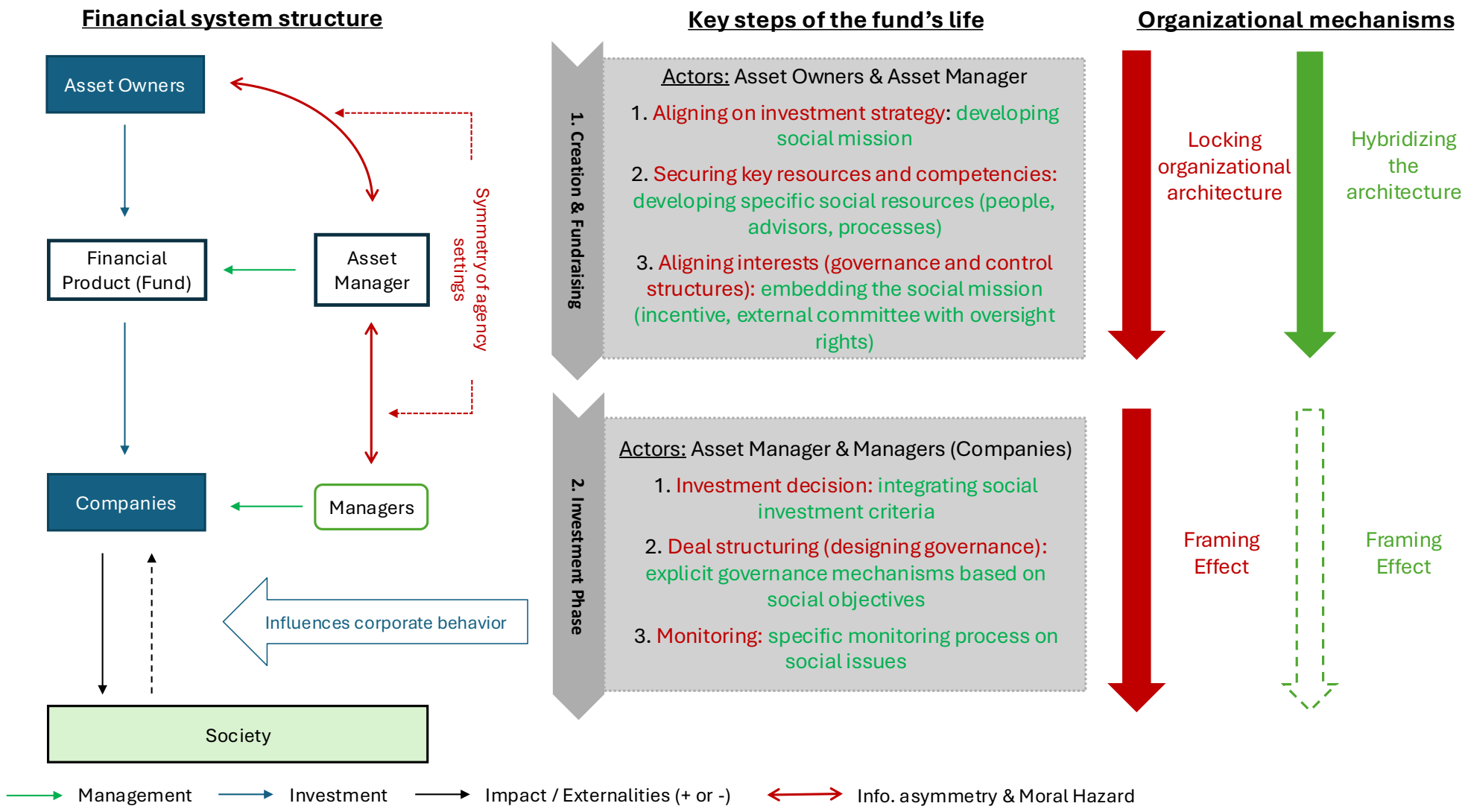

Figure 7: Simplified processual model - Hybridizing investment organizations

Note: This simplified process model presents the modern financial system's organization (left side) and our results & contribution (right side).