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Corporate Governance and Corporate Law Structure in European Countries

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Abstract

The paper describes the different broad systems of corporate governance existing in Continental Europe (the insider system) and in the UK (and the US, the outsider system), identifies certain differences in the concentration and nature of corporate ownership between both systems and comments on the consequences that these discrepancies have in terms of agency costs and the development of mechanisms to separate ownership (cash flow rights) and control (voting rights) both at the level of the firm and through corporate law. Then, a reference is made of the important question of whether corporate governance structures in the different European countries will competitively converge with one another. To than end, proper amendments in corporate structures, most notably corporate law reform, must be initiated.

Keywords: corporate governance, corporate law, Europe

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1. Introduction

Corporate ownership and governance structures differ greatly among the European economies. Some firms in the member-states are characterized by diffused ownership and managerial control, others by mostly concentrated ownership and still others by considerable stakeholder influence in the firm. As Bebchuk and Roe (1998) point out, an important question in modern corporate ownership and governance debates throughout the world is whether corporate structures in countries at a similar stage in their economic development will converge with one another? The question is most important in Europe. On the one hand, the forces inducing convergence in corporate governance seem powerful: product and capital markets competition, discovery and dissemination of best practices, rapid information flows across national boundaries. On the other hand, there exist powerful forces, which impede convergence, with the most powerful impediments rooted in path-dependence processes and other institutional factors.

Corporate ownership and governance structures depend on corporate rules; hence, convergence of corporate structures depends to a large extent on the convergence of corporate rules. Thus, for structural convergence to occur on a

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European scale, the advanced European economies' corporate rules must converge. However, because of powerful path dependent and other institutional reasons corporate rules in the advanced European economies might not converge. Even if state bureaucracies are efficient, a country's corporate rules might be path dependent, as they depend both on the country's initial corporate governance structures, including tradition, interest group politics and foreign features. The initial pattern of a country's corporate structures has created interest groups and accordingly determined their power to influence the pattern of evolution of corporate law rules. If a pattern of ownership and governance creates a group with positional advantage inside the firm and society, that group will often have the motivation and the means to preserve rules that favour itself.

Consequently, the rules that a country will have down the road will depend on the type of corporate structures and corporate rules that it began with. Once a country has rules that favour, for example, powerful professional managers over shareholders or other corporate constituencies, these managers will want to fight off a change in rules and often they will have the resources to do so. Similarly, a country whose rules favour, for example, concentrated shareholders will have a powerful interest group, namely the concentrated owners, who will want to fight off a change in rules. And similarly, a country whose rules favour stakeholder participation will not easily reverse course.

Moreover, depending on the initial corporate conditions, the efficiency of local structures is often path dependent: sunk adaptive costs and network externalities may impede structural change. Furthermore, even inefficient structures may tend to persist, owing to an insufficiently high level of transactions activity that could act as a catalyst for structural transformation. Thus, if higher transactions activity in a firm results in a reduction of the firm's controlling shareholder's wealth, then the controlling shareholder might impede the firm from further diffusing ownership, even if diffusion would be overall efficient for the firm. And management might impede their firm from moving to concentrated ownership even if moving there would be overall efficient. Thus, the question is whether the powerful forces of our rapidly globalizing product and capital markets will succeed in inducing adequate structural change and convergence.

Thus globalisation, competition, and rules reform put pressure on firms to change and adopt more efficient governance practices. But, equally, firms face powerful pressure to stay on their prior path, so the resultant speed and direction of change would then be an empirical question and, given the strength of the forces of persistence, it is doubted whether the result will be complete and rapid convergence, and a wide variety of different structures will tend to persist.

The issue of convergence of corporate ownership and governance structures is not only important at the state level but also at the investor and capital market practitioners level with respect to devising efficient investment strategies in the modern complex world. Indeed, traditionally share price returns and their variance have been explained by factors linked to the economic operations of the company such as systematic risk, corporate size and P/E ratios (as in Fama and French, 1992) or by factors related to the influence of the macro-economic environment. In these models, the institutional environment in terms of concentration and nature of voting rights, bank debt dependence and corporate and legal

mechanisms to change control have rarely been included. Crama et al. (2000) argue that empirical research on the dynamics of ownership and its impact on corporate performance in European economies has become possible only in recent years, given that the European Commission's Transparency Directive of 1988 (88/6278EC) has only gradually been integrated into the national legislation of continental European countries. It is well known that EU states retain the right to implement the Commission's directives according to their own existing structures and specific requirements. As a result, corporate ownership and governance rules differ substantially across EU states in terms of statutes, notification thresholds and frequency.

The purpose of the paper is, first, to highlight aspects of the discrepancies among the different corporate governance structures and, second, to present some evidence on the different corporate law structures in the European states. Within Europe, the corporate law landscape is particularly interesting because of its widely diverging nature and liquidity of the market for controlling rights.

The paper is organised as follows. Section 2 discusses the main differences in ownership structures in Europe. The section draws upon the research results of the European Corporate Governance Network. Section 3 provides information on voting rights in the different European corporate governance frameworks and highlights the role of corporate law, minority protection, and legal structures. Section 4 focuses on a key issue in any economic analysis of corporate governance, i.e. the analysis of the corporate law structures of the European states and finally section 5 offers some conclusions.

2. Ownership Concentration and Voting Blocks

2.1 Insider Versus Outsider Corporate Governance Systems

Drawing on Crama et al. (2000) and the European Corporate Governance Network studies, some interesting features emerge from the comparison of corporate structures in the EU, despite the lack of detailed data availability. Major differences in ownership concentration between continental Europe and the Anglo-American countries are highlighted in Table 1. The evidence shows that ownership concentration is relatively higher in the continental Europe. Large shareholders as a whole own more than 60 percent of the voting rights in joint stock companies in the former and only about 40 percent in the latter. On the other hand, large individual shareholders own on average higher voting rights in the continental Europe than in the Anglo-American countries: the largest owner in the median UK listed company holds a stake of less than 15 percent and this stake is less than 5 percent in the US. In contrast the largest shareholder (or group of large shareholders) controls 40 to 54 percent of the voting rights on the continent. About 85 percent of the listed non-financial companies in Continental Europe have a large shareholder, who holds at least a blocking stake, whilst in about 50 percent of the companies, the large shareholder owns an absolute majority.

Table 1: *Concentration of voting rights by country*

	ECGN Studies (1998)	Num. of companies in the sample	Disclosure Threshold	Total ownership concentration		Largest shareholder	
			%	Mean	Median	mean	median
Austria	Gugler, Kalss, Stomper,Zechner	50 listed (all)	5	65.5	60.0	54.1	52.0
Belgium	Becht et a1	150 listed (all)	5	63.4	66.5	55.8	55.5
France	Bloch and Kemp	40 listed (CAC) (1)	5	52.0	30.0	29.4	20.0
Germany	Becht and Boeh-mer	374 listed (all) (3)	5	<65%	<65%	η.a.	52.1
Italy	Bianchi, Bianco, Enriques	216 listed (all)	2	68.4	62.3	51.9	54.5
Netherlands	De Jong, Kabir, Mara	137 listed (all)	5	62.5	69.8	42.8	43.5
Spain	Crespi, Garcia-Cestona,	193 listed (all)	5	65.1	63.2.	40.1	34.2
UK	Goergen et al.	250 listed (2)	3	40.8	39.0	15.2	10.9
US	Becht et a1.	1309 (NYSE)	5	ca 30%	n.a.	< 5%	< 5%

Source: Barca and Becht (1999).

The pattern of concentration ownership provides the basis for the distinction between an insider and an outsider system of corporate governance. High ownership concentration characterizes the insider system. In the latter, the corporate sector has controlling interests in itself because companies have grown to multi-branch financial conglomerates; the number of listed companies is small compared to the size of the economy; and the capital market is illiquid and therefore small because controlling blocks are held by a few dominant shareholders. Moreover, as Renneboog (2000) points out, in spite of all the efforts made to simplify corporate structures, a large number of holdings or interlocked companies remains, which de facto deter any attempt by outsiders to control any of them. Thus, while corporate law in an insider system usually offers the opportunity to participate in company earnings, outside investors have little hope to trade and acquire control.

In contrast, low ownership concentration characterizes the outsider system, which is dominant in the Anglo-American countries. In that system, the number of listed companies is large; the right to participate in company earnings is extended, as is the ability to acquire control of the company's equity capital. The outsider system is effectively market-oriented, that is, characterized by a liquid capital market with frequently traded ownership and control rights. Corporate structures are characterized by the existence of few corporate holdings or interlocked patterns of ownership. Finally, there are few major, controlling shareholdings and these are rarely associated with the corporate sector itself (Wymeersch, 1994, Franks and Mayer, 1995).

The relative efficiency in providing economic benefits and securing adequate accountability to shareholders and society has also been a major object of concern regarding the insider and outsider systems. As Allen and Gale (1995) argue, the former systems proved historically more efficient in diffusing risks over time, whilst the latter systems proved historically more efficient in diffusing risks across sectors or countries.

2.2 Cash Flow Versus Voting Rights

The studies in the E.C.G.N. show that equity markets in Continental Europe display both quantitative similarities but some qualitative differences. Indeed, as shown in Table 1, the nature of the main shareholders varies from country to country. Obviously, each category of shareholder has different incentives or abilities to exert control. For example, there is little evidence that institutional investors undertake any disciplinary actions against poorly performing management (Stapledon, 1996). In contrast, corporate shareholders might value dominant shareholding positions, not only for the financial return of their investment, but also for other potential benefits of control, especially when a customer or supplier relation exists with the target company (Barclay and Holderness, 1989).

Moreover, the complexity of ownership structures also varies across countries (see also Cramer et al, 2000, reporting on E.C.G.N.). Germany, for example, is characterised by complex shareholdings around and within industrial groups while the French system is characterised by ownership cascades of financial groups and cross-company shareholdings. In Italy, long pyramids controlled by state or family-owned corporations are typical. More than a third of listed and non-listed Belgian companies are controlled by financial holdings companies while in most Dutch listed companies, the separation of ownership and control is almost absolute, as blocks of voting rights are not held by shareholders but by an Administration Office. Finally, although state controlled ownership has decreased substantially in Spain since 1995, state holding companies still own a golden-share in strategic sectors.

These differences reflect different corporate law structures and have important implications in terms of the one-share-one-vote principle. Ownership pyramids, for instance, manifested in financial conglomerates, allow power concentration with limited investment, since controlling a target company can be achieved via a number of subsidiaries and a chain of absolute majority of their voting rights. In financial conglomerates, with one intermediate holding, the ultimate shareholder retains absolute control while receiving only 25 percent (=0.51x0.51) of the cash flow. Thus, cash flow rights are not the same as voting rights, since through control leverage one may detain control over a large number of entities while only investing small sums and being entitled to only a small portion of cash flows. Whereas legal restrictions have impeded the occurrence of ownership concentration in the UK, they are common practice in Continental European states. Another way of amassing voting power is through voting pacts and proxy votes. For example, voting pacts are not uncommon in Germany (Chirinko and Elston, 1995) and German banks commonly use proxy votes of the shares deposited in their custody (Wenger and Kaserer, 1997).

Still, a number of mechanisms exist to erode voting power, such as the imposition of voting caps. An extreme case is the Netherlands where under the prevailing 'structural governance regime', non-voting certificates are distributed to ordinary shareholders while the voting power is given to a foundation controlled by company insiders (De Jong et al, 1998). In Germany, Belgium, Spain or Greece, a decision by the board of directors can limit any percentage of voting power to e.g. 5 percent. Usually, the board of directors can install voting caps after prior concern of the annual general meeting, which may approve it for a certain period of time and under certain conditions. Whereas dual class shares are frequently used to separate ownership and control in Sweden (Agnblad et a1, 1999), this has been actively discouraged in the UK by the LSE (Brennan and Franks, 1997). Finally, since the take-over wave in the 1980s, several anti-takeover devices, such as poison pills including shelf registration of equity, issuing bonds cum warrants or convertible bonds, are frequently used to dilute the voting power of 'hostile' shareholders (see the recent attempt by the Euronext to act as a 'white night' in order to prevent the hostile takeover of LSE from the Swedish OM exchange that has resulted in the seemingly failure of the iX merger). With prior consent by the shareholders at an annual meeting, the board of directors can issue new equity, place it with 'friendly' shareholders and thus dilute the share stakes of other shareholders.

2.3 Corporate Governance and Agency Costs

Both the insider and outsider corporate governance systems present weaknesses and advantages, which can be analysed in terms of the principal-agent theory (see Table 2). The Anglo-American system, characterised by high dispersion of voting and cash flow rights, leads to weak owners and strong managers and may induce free riding on control (Shleifer and Vishny, 1986, 1997; Roe, 1994; Hart, 1995b, among others). As a single small shareholder only benefits from performance improvements in direct proportion to the cash flow rights, he or she may not find it profitable to monitor management while a large shareholder will necessarily feel differently. This situation may result in agency conflicts between management and shareholders. Law monitoring resulting from voting rights dispersion might be counterbalanced by increased bank monitoring (Edward and Fischer, 1994, 1998). Still, the large free float allows investors to take advantage of portfolio diversification possibilities and introduces the discipline of the (hostile) take-over markets (Martin and McConnel, 1991; Franks and Myer, 1996).

Concentration of ownership and voting rights, on the other hand, stimulates corporate governance actions against under-performing management, but may lead to expropriation of the rights of minority shareholders (lower right segment of Table 2. Furthermore, share liquidity is reduced due to the low free float and hostile take-overs are virtually ruled out.

Table 2: *Ownership and voting power: Structure and consequences*

	Dispersed Ownership and Dispersed Voting Power	Dispersed Ownership and Concentrated Voting Power	Concentrated Ownership and Dispersed Voting Power	Concentrated Ownership and Concentrated Voting Power
Where	UK, USA	Countries where a stake holder can collect proxy votes and shareholder coalitions are allowed	Any company with voting right restrictions	Continental Europe, Japan, in any company after take over
Advantages	- Portfolio diversification and liquidity - Take-over possibility	- Monitoring of management - Portfolio diversification and liquidity	Protection of minority rights	High monitoring incentives
Disadvantages	- Insufficient monitoring - Free riding problem	- Violation of one-share-one-vote - Reduced take over possibility	- Violation of one-share-one-vote - Law monitoring incentives, - Law portfolio diversification possibilities and low liquidity - Higher cost of capital - Reduced take over possibilities	- Low portfolio diversification possibilities and low liquidity - Reduced take over possibilities
Agency conflicts	Management vs. shareholders	Controlling block holders vs. small shareholders	Management vs. shareholders	Controlling block holders vs. small shareholders

Source: E.C.G.N.

The upper right and lower left segments of Table 2 present the other combinations of concentrations of ownership and voting rights which can be attained by some of the instruments described above to amass or dilute voting power. For example, when shareholder coalitions or proxy votes are allowed, the supervisory power of a

block of shareholders vis-à-vis management increases, but the agency conflicts shift from shareholder-management towards large versus minority shareholders.

3. Corporate Governance, Financial Markets and Corporate Law.

The discussion above clearly points to the difficulty in explaining corporate governance systems on the basis of conventional theories. In this section, we shall emphasise this critical point before moving on to a discussion of the methodology we use to measure control.

Indeed, neither transaction costs theory (Coase, 1937; Williamson, 1983), nor principal agent theory (Jensen and Mechling, 1976; Milgrom and Roberts, 1992), nor the theory of implicit contracting (Grossman and Hart, 1982, 1986; Hart and Holmstrom, 1987; Hart and Moore, 1988; Hart 1995a) nor the theory of vertical integration (Alchian and Demsetz, 1972) can fully explain why two governance systems (Continental European and Anglo-American) have emerged or, in a more refined way, why Continental European countries differ in terms of structure and concentration of ownership (cash flow rights) and voting rights. In the previous section, we have shown that the weaknesses of both systems have been partially dealt with through mechanisms separating cash flow and voting rights. In addition however, governments have often found it necessary to develop a legal environment able to limit the inconveniences (e.g. agency costs) induced by the corporate governance system.

In fact, historic evolution of regulation has shaped ownership structures, capital markets and corporate governance systems. Not surprisingly, there are two broad legal traditions; the common law system, found in Anglo-American countries and the Commonwealth, and the civil law tradition of Continental Europe and its sphere of influence (former colonies). These two legal systems are different in terms of shareholder protection, adherence to the one-share- one-vote principle and creditor protection. According to La Porta et a1. (1996, 1997), the common law system appears to provide stronger shareholder and creditor protection, even though as Franks et al (1998) show there considerable differences in corporate control mechanisms. But legal distinction can explain differences in corporate governance systems and the degree of capital market development. In common law countries, the ratio of external capital to GDP is higher, as are the ratio of corporate debt to GDP and the number of listed domestic firms and initial public offerings as a proportion of the corporate population. Whether or not the institutional environment has a momentous impact on economic activity has been explored by a number of authors. In particular, Carlin and Mayer (1998) investigate the relation between economic growth, R&D investment and fixed income formation, on the one hand, and the presence of bank-firm relations, development of security markets, degree of ownership concentration and the legal system on the other. For a sample of companies in 20 countries, there is little influence of banking activity and ownership concentration on economic growth, but they find that legal protection of investors and development of securities markets matter.

A seemingly logical implication of the discussion above is that it would be extremely difficult to develop a set of corporate governance regulations applicable to all EU countries without undertaking the difficult task of concomitantly dis-

mantling the existing country-specific mechanisms that currently provide shareholder protection. Indeed, several attempts made in that direction had to be withdrawn. For example, the mandatory take-over bid requirement for all listed companies included in the first draft of the 3rd Company Law Directive was dropped. The consequence would have been a weakening of direct monitoring resulting from reduced voting block sizes (Becht, 1999). The 6th Company Law Directive (now abandoned as well) aimed at imposing the one-share-one-vote rule on all European companies. As dual class shares would also have been ruled out, there was a danger that shareholders would have reacted by relying increasingly on pyramids and voting pacts in order to retain control, thereby reducing market liquidity.

Detailed information on existing corporate law structures in the OECD countries is presented in Tables 3 to 5, based on recent OECD data. Table 3 shows that only three OECD countries have adopted the one-share-one vote rule, whilst mail voting and cumulative voting is possible in about 25 percent of them. Rules preventing the blocking of shares before the general meeting can in general be found in the advanced capitalist countries. Oppressed minority shareholder protection is found in only a few countries as well, whilst strong pre-emptive rights are mostly found in the less advanced OECD countries.

Table 4 presents data on creditor protection. As the summary index column shows strong creditor protection is found in the Germanic countries (Austria, Denmark, Germany) owing to the traditionally important role of credit institutions in corporate control as well as in Korea. On the other hand, the UK and New Zealand figure exceptionally high in the index. This might be explained by the special character of the relationship between financial and industrial capital traditionally prevailing in those countries as well as the emphasis given to securing an integrated corporate governance system.

Table 5 presents information on investor protection levels in the OECD. The last column of the table shows that stronger investor protection, as defined by the weighted average of the rest of the indices, is found in the Nordic countries and the UK. The Germanic countries figure at low levels, owing to their traditional mode of corporate finance and control. Surprisingly, relative small investor protection level is found in the US. Finally, low investor protection levels characterize the less developed markets of Greece and Portugal.

As can be seen, several differences exist in corporate law rules among the OECD member-states as far as shareholder rights, creditor rights and disclosure and transparency levels are concerned. Even thought the information provided may not represent the full picture of incorporation law in the OECD countries, which is subject to considerable alteration as a result of the recent initiatives in corporate law reform by those countries, it presents a good account of the existing differences. These differences set the agenda for the required corporate law reform, to which we turn next.

4. Corporate Governance and Corporate Law Reform.

As it was pointed out in the introduction, it is essential for the sound development and international competitiveness of European corporations if a certain degree

of convergence in governance structures is achieved, which will largely be manifested through proper changes in corporate law rules. Essential element in the direction of these changes should be that the board should thoroughly supervise corporate management and be held accountable for that to the general shareholder meeting. In addition, the corporations should ensure more active functions of the board, wider representation and the transparency of corporate management.

Thus, the implementation of regulatory reforms to improve corporate governance must be initiated. Proper amendments in corporation law and the empowerment of the competent regulation authorities to enforce them will contribute to the realization of reform. Other financial industry related laws must also be amended as to incorporate several recommendations from the codes of best practice for corporate governance that have sprung all over Europe.

These reforms must focus on the expansion of the quantity and quality of information disclosure, the increase in the number and powers of outside directors in the boards and the introduction of audit committees in full charge of auditing. The gradual adoption of these new structures is the result of a strong urge by the European Commission, the OECD and other international organizations, by domestic and foreign institutional investors as well as by the recognition of inefficacy of existing corporate management auditing procedures.

The question at hand is the direction to which corporate law structures must be reformed in order to alleviate those differences. To that question, virtually all committees on corporate governance, established in European states with the purpose of providing recommendations for best corporate governance and practice, respond that new basic concepts, terms and conditions need to be introduced for the development of a modern and efficient corporate governance framework.

The required amendments in the corporation law of the European countries should, in general, be based on the following principles: ***(a)*** a clear definition of and separation between rights and responsibilities of the corporation's different governance bodies must be maintained, ***(b)*** shareholders should be encouraged to maintain their investment in the company, ***(c)*** the board of directors should rather be characterized by a two-tier structure, ***(d)*** minority shareholders should be properly protected and their views adequately represented, ***(e)*** shareholders, specially in smaller companies, should be given the opportunity to selectively amend rules, without however causing an unlawful breach of these rules and provisions.

More specifically, several suggestions are made for the amendment of corporation law, which include the following: Amendments must be made in the direction of share issuance procedures. It is recommended that only one class of common shares with a general right to vote should be issued. However, exceptions may be allowed in the direction of strengthening minority shareholder rights.

Serious attention should be given to the need for the gradual abolition of bearer shares in favour of registered shares. The completion of the 'dematerialization' of listed securities in most European stock exchanges has already resulted in their de facto registration, so their de jure abolition seems a natural consequence. Moreover, the existence of bearer shares is in general associated with considerable risks, such as the risk of fraud in the sale of forged certificates that purport to represent bearer shares, the risk of theft of those shares left in paper form or belonging to non-listed companies, the risk that controlling

shareholders may use bearer shares to hide their control over a company and, finally, the difficulties of voting associated with the existence of bearer shares since distant or electronic voting is not possible.

A considerable strengthening of shareholders pre-emptive rights must be established in order to secure the shareholders' fair treatment when large changes in corporate capital structures are under way. Strong pre-emptive rights should however be matched by the establishment of appropriate 'participation rights', allowing shareholders who vote against a waiver of pre-emptive rights to be treated equitably and fairly.

The structure of the board of directors must be properly changed as to provide a proper balance between accountability and enterprise. This requires the selective but explicit establishment of a two-tier board structure with both a supervisory board of directors elected by and being accountable to the shareholders and a management board appointed by the supervisory board.

The explicit establishment of both non-executive (outside) members in the board and a sub-committee system for the board is crucial. The board, for its operational efficiency, should be required to establish internal committees, which include a minimum number of independent directors, and delegate their authorities to the committees. The board should also be required to have an internal audit committee that includes a minimum of three directors for securing auditing efficiency. Outside directors of the internal audit committee should represent the majority of the total committee members and have authority equivalent to that of an existing auditor. The establishment of auditing procedures, if it is to prove efficient, should be accompanied by proper information disclosure practices, which, in turn, require among other things the establishment of proper accounting standards.

The board should also be required to establish a remuneration sub-committee that also includes outside directors as members. The sub-committee should be endowed with sufficient authority and access to information to settle on remuneration contracts of management and the board approved by the shareholders, the terms and conditions for the use of executive share options and examine the associated risk undertaken by the corporation.

Controlling shareholders, who practically exercise managerial powers to influence and control managerial decision procedures, must bear the corresponding legal responsibilities for their participation in management decisions. This involves a reduction in the level of limited liability enjoyed by controlling shareholders. In this respect, the company's relation with its creditors is particularly important.

The voting rights of minority shareholders should be strengthened to encourage the efficiency of shareholders' oversight of corporate management and to ensure its transparent operations. The minimum level of share ownership required to exercising minority shareholders' rights should be reduced as a percent of outstanding shares. Given the expansion of derivatives transactions, the amendment of corporation law should also specify a hurdle level of share holding for raising a derivative suit.

A cumulative voting system should be established. Cumulative voting, if so desired, might be selectively adopted so that directors who represent minority shareholders' interests can be elected. This means that each share should be allowed to have the same number of votes as the number of directors to be

elected, in the case of shareholder with less than a certain minimum of outstanding shares.

New voting procedures should be established that include the possibility of postal or electronic ballot in order to better and more widely reflect opinions of minority shareholders in the general meeting of shareholders. Changes in the procedures regulating the board meeting should be established as to allow directors to attend the meeting not only in person but also through teleconference procedures.

Even though directors' responsibility is established, it could nonetheless be further strengthened, in particular with regards to recording in detail the board meeting views of directors who opposed certain agenda and the reasons for the opposition. Also shareholders should be allowed to read and copy the details.

Serious consideration should also be given to establishing proper procedures governing takeover activity in the market and securing the accountability of management to the board and them both to the general shareholder meeting.

5. Conclusion

This paper has described two broad systems of corporate governance existing in Continental Europe (the insider system) and in the UK (and the US, the outsider system). Certain differences in the concentration and nature of corporate ownership between both systems are described. For example, in a typical Continental European country, (majority) control is held by one shareholder or a small group of interlocked (corporate) shareholders, whereas Anglo-American companies are predominantly widely held. These discrepancies have important consequences in terms of agency costs and therefore mechanisms have been developed in most countries to separate ownership (cash flow rights) and control (voting rights) both at the level of the firm and through corporate law.

The corporate governance structures in Europe have been undergoing considerable reform in terms of statutes and regulations. An important question in this respect is whether corporate governance structures in the different European countries will eventually converge with one another. To than end, proper amendments in corporate structures, especially legal structures, must be initiated. However, as the conclusions of empirical research have shown and, most importantly, the recommendations by the corporate governance committees set up all over Europe have emphasized, efficient corporate structures will established if the governments and other competent capital market authorities expend all necessary effort to implant the need for competitive governance into corporate minds. This ongoing effort is required for modern corporations in order to survive in the globally competitive era.

Consistent implementation of structural reforms is required, in order to make national economic structures internationally competitive. Further improvements in existing European corporation law as it relates to governance structures are required, including plans for strengthening the rights and responsibilities of the board and outside directors, strengthening shareholders' rights, supervising transactions with related parties, ensuring the effectiveness of shareholders' exercise of rights, expanding the level of corporate disclosure, encourag-

ing institutional investor's active involvement in corporate governance and setting clear procedures for mergers and acquisitions.

Most importantly, corporate minds must be willingly receptive and adopt proper practices on corporate governance. It will not pay-off European corporations to keep old-fashioned mentalities and stick to inefficient previous practices. Instead, they should be proactive to stand along with global standards, which is a key element in surviving in the new unlimitedly competitive environment. It should be recognized that this is the only way to maximize shareholders' interests and companies' values.

As institutional funds and pension funds are increasingly asserting their role in the European capital market, fund managers get in a position to supervise corporate management. As such, they should take an active participation in supervising corporate management by way of nominating or discharging managers in cooperation with the outside directors.

Directors, internal committees and controlling shareholders should all have legal responsibilities as regards the efficiency of overall corporate management structures so that their systematic and efficient operation is ensured. Otherwise, moral hazards may be in place. Related rules need be further reformed such that responsible persons shall take on their corresponding legal liabilities. It must also be noted, and this is nowadays an issue of rising importance in the western world with increasing derivatives transactions, that the conditions for exercising derivative suits must be properly set.

It must also be noted that private organizations representing shareholders interests should be further encouraged to actively watch the actions of corporate management. Their activity, which should be motivated by economic justice and proper business ethics, has indeed been growing. Such organizations have played important and positive roles in raising concerns toward the improvement of prevailing corporate governance structures. It should be noted, however, that for an eventual success of those activities, shareholders and their organizations should undertake strong action in claiming and defending their rights by themselves.

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Table 3: *Shareholder rights in OECD countries*
(1 = shareholder protection is in the law)

Country	One share = One vote	Voting by mail allowed	Shares not blocked before meeting	Cumulative voting / proportional rep-res/tion	Oppressed minority protection	Pre-emptive right to new issues	% of share capital to call an extraordinary shareholder meeting[1]	Summary index
Australia	0	1	1	0	1	0	5	4
Austria	0	0	0	0	0	1	5	2
Belgium	0	0	0	0	0	0	20	0
Canada	0	1	1	1	1	0	5	5
Denmark	0	0	1	0	0	0	10	2
Finland	0	0	1	0	0	1	10	3
France	0	1	0	0	0	1	10	3
Germany	0	0	0	0	0	0	5	1
Greece	1	0	0	0	0	1	5	3
Ireland	0	0	1	0	1	1	10	4
Italy	0	0	0	0	0	1	20	1
Japan	1	0	1	1	1	0	3	5
Korea	1	0	0	0	1	0	5	3
Mexico	0	0	0	0	0	1	33	1
Netherlands	0	0	0	0	0	1	10	2
New Zealand	0	1	1	0	1	0	5	4
Norway	0	1	1	0	0	1	10	4
Portugal	0	0	1	0	0	1	5	3
Spain	0	0	0	1	1	1	5	4
Sweden	0	0	1	0	0	1	10	3
Switzerland	0	0	0	0	0	1	10	2
Turkey	0	0	1	0	0	0	10	2
U.K.	0	1	1	0	1	1	10	5
United States	0	1	1	1	1	0	10	5
Means:								
Overall	0.13	0.29	0.54	0.17	0.38	0.58	10	2.96
G7	0.14	0.57	0.57	0.43	0.57	0.43	9	3.57
EU[3]	0.07	0.14	0.43	0.07	0.21	0.79	10	2.57
Euro 11[3]	0.00	0.10	0.30	0.10	0.20	0.80	10	2.30

Source: OECD, La Porta et al (1998)

Table 4: *Creditor rights in OECD countries*
(1 = creditor protection is in the law)

Country	No automatic stay on assets	Secured creditors first paid	Restrictions on going into reorganisation	Management does not stay in reorganisation	Summary index
Australia	0	1	0	0	1
Austria	1	1	1	0	3
Belgium	1	1	0	0	2
Canada	0	1	0	0	1
Denmark	1	1	1	0	3
Finland	0	1	0	0	1
France	0	0	0	0	0
Germany	1	1	1	0	3
Greece	0	0	0	1	1
Ireland	0	1	0	0	1
Italy	0	1	1	0	2
Japan	0	1	0	1	2
Korea	1	1	0	1	3
Mexico	0	0	0	0	0
Netherlands	0	1	1	0	2
New Zealand	1	0	1	1	3
Norway	0	1	1	0	2
Portugal	0	1	0	0	1
Spain	1	1	0	0	2
Sweden	0	1	1	0	2
Switzerland	0	1	0	0	1
Turkey	0	1	1	0	2
U.K.	1	1	1	1	4
United States	0	1	0	0	1
Means:					
Overall	0.33	0.83	0.42	0.21	1.79
G7	0.29	0.86	0.43	0.29	1.86
EU[1]	0.43	0.86	0.50	0.14	1.93
Euro 11[1]	0.40	0.90	0.40	0.00	1.70

Source: OECD, La Porta et al (1998)

[1] Countries in sample.

Table 5: *Framework conditions: enforcement and transparency* (Indices)

	Observance of laws and regulations		Efficiency of the judicial system	Risk of contract repudiation	Rating on accounting standards	Policy effective-ness	Memo item: compound measure of investor protection[1]
	(a)	(b)	(a)	(b)	(a)	(c)	
Australia	10.00	8.19	10.00	7.92	8.71	75	0.60
Austria	10.00	8.62	9.50	7.44	9.60	54	0.24
Belgium	10.00	6.59	9.50	6.77	9.48	61	-0.29
Canada	10.00	8.10	9.25	8.43	8.96	74	0.62
Denmark	10.00	8.38	10.00	8.44	9.31	62	0.76
Finland	10.00	8.47	10.00	8.27	9.15	77	0.56
France	8.98	7.15	8.00	7.56	9.19	69	-0.61
Germany	9.23	7.97	9.00	7.82	9.77	62	0.23
Greece	6.18	5.99	7.00	6.12	6.62	55	-3.19
Ireland	7.80	7.79	8.75	7.72	8.96	742	-0.22
Italy	8.33	6.72	6.75	6.55	9.17	62	-0.95
Japan	8.98	7.84	10.00	6.68	9.69	65	-0.52
Korea	5.35	0.94	6.00	0.41	8.59	62	
Mexico	5.35	-0.47	6.00	0.18	6.55	60	
Netherlands	10.00	8.17	10.00	9.06	9.35	64	0.53
New Zealand	10.00	8.65	10.00	8.14	9.29	70	0.66
Norway	10.00	8.67	10.00	8.33	9.71	74	1.02
Portugal	8.68	7.17	5.50	7.30	8.57	36	-1.28
Spain	7.80	7.06	6.25	8.21	8.40	64	-0.96
Sweden	10.00	8.25	10.00	8.15	9.58	83	0.82
Switzerland	10.00	8.99	10.00	8.97	9.98	68	0.72
Turkey	5.18	-0.01	4.00	-0.41	5.95	51	
U.K.	8.57	8.38	10.00	8.93	9.63	78	0.86
United States	10.00	7.51	10.00	7.73	9.00	71	0.42
Means:							
Overall	8.77	6.88	8.56	6.86	8.88	65	0.00
G7[3]	9.16	7.67	9.00	7.67	9.34	69	0.01
EU[3]	8.97	7.62	8.59	7.74	9.06	64	-0.25
Euro 11[3]	9.08	7.57	8.33	7.67	9.16	62	-0.28

Source: OECD, based on information provided for (a) by La Porta et al (1998), for (b) by Kaufmann et al (1999), for (c) by CIFAR (1995).

Note: Variables are defined in Annex 2. Higher scores indicate stronger contract and law enforcement and greater transparency. Scores can range from zero to 10 for enforc ement and zero to 100 for the rating on acco unt standards.

1 The measure of investor protection is the first principal component of legal enforcement and transparency variables as stated in this table, as well as shareholder and creditor rights' variables (Tables 1 and 2).

2 For Ireland, "Rating on accounting standards" is based on industrial companies only.

3 Countries in sample.