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The Corporate Governance "Codes of Conduct" between state and private law

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Abstract

The relationship between corporate governance codes and the legal order in which they function is a complex one. This paper aims at analysing this relationship on the one hand by describing the factual situation in which the codes have been developed, and on the other the enforcement and monitoring of the codes in the different jurisdictions. It points to the weaknesses in enforcement and calls for developing stronger enforcement instrument without abandoning the self-regulatory nature of the codes

The Corporate Governance "Codes of Conduct" between

state and private law

Eddy WYMEERSCH[1]

A. Introduction

1. Corporate governance has been a core matter since the times that economic activity was exercised in company form. The fundamental agency problem has always been present in one way or another and contract clauses, or charter rules were needed to streamline the relationship among the partners, or later between the shareholders and the board. Over time, as the agency relationship became more distant there was an increasing need to extend the reach of these agreements. In listed companies the need for clear corporate governance arrangements is greater as shareholders have little impact on boards, while risks for self dealing and conflicts of interest increase. In companies with concentrated ownership, a comparable conflict relates also to the relationship among the shareholders, especially the controlling or dominant ones, and the investing public.

2. Before the introduction of additional corporate governance mechanisms in the codes, the company law in the various countries contained already sometimes quite elaborate governance provisions. Boards were mostly mandatory, rules on appointment and especially dismissal, on the remit and functioning of the board, the election of a chairperson, etc. were all part of the traditional company laws. These rules have remained in place although changes have been introduced in the law of many Member states to clarify or redefine provisions that were already in the law.

The European directives have not dealt with the governance issue as such[2]: a number of diverse provisions deal with partial aspects, and these are of course not without importance[3]. A recent directive now deals with the governance codes, as will be explained later on.

It should be stated from the outset: the present analysis only deals with companies that are traded on regulated markets, and with the codes of conduct that are applicable to them. Codes addressing unlisted companies raise other questions, but have been left out, brevitatis causa.

B. The Corporate governance normative instruments: an overview

3. Before starting an analysis of the governance codes phenomenon, it seems useful to give an overview of the present situation in at least a number of EU member states. These codes are all posted on the website of the European Corporate Governance Institute. Some international developments serve as introduction.

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[1] Professor at the Ghent Law Faculty; member of the European Corporate Governance Forum.
[2] At one time, governance rules were proposed in the so-called 5th directive (Amended Proposal, Com (90), 629, Final, OJ C 7, 11 January 1991.
[3] One should especially mention here the rules on auditors and on audit committees (esp. the Eighth Directive as amended, and the mandatory bid rule (art. 5, Directive, 2004/25 on takeover bids of 21 April 2004).

1°. The international level

(a) The OECD

To start with the international level, one should refer to the OECD Principles of Corporate Governance 2004 which contain high level guidelines to which national corporate governance initiatives should respond, whether by way of laws and regulations or through other instruments like the codes[4]. Much attention is paid to the position of the shareholders and other stakeholders while the board's position is analysed from the angle of its relationship to the management, its accountability and the relationship with the shareholders. The OECD has made very considerable efforts to convince governments, business practitioners and other opinion leaders of the need to adopt its standards. A targeted assessment document has been developed and is used by the IMF in its ROSC (Reports on the Observance of Standards and Codes) programmes for assessing national corporate governance systems. The Financial Stability Forum has listed the principles among the 12 most important standards for a sound financial system[5]. The OECD principles have been established by representatives of the national ministries, with the contribution of the Business and Industry Advisory Committee and the Trade Union Advisory Committee. They were originally approved by the OECD ministers in 1999 and a revised version was released in 2004.

(b) The Basel Committee

The Basel Committee has issued a guidance on corporate governance for banking organisations.[6] It is not intended as an additional layer of regulation, but as a guidance for banks required to adopt and implement sound corporate governance practices. The role of the banking supervisors in assessing sound practices is highlighted.

(c) IOSCO

A working party within IOSCO has recently started studying corporate governance subjects, such as defining director's independence.

(d) EBRD

The EBRD has adopted "Sound business standards"[7] more explicitly addressed to transition economies in Central and Eastern Europe and Russia. The relationship with local communities and governments deserved special attention.

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[4] OECD Principles on corporate governance, published by OECD; see L. Boucher, The OECD Principles of Corporate governance, Ondernemingsrecht, 2006, 378.

[5] http://www.ebrd.com/country/sector/law/corpgov/standard/index.htm

[6] Enhancing Corporate governance for banking organisations, 13 February 2006. http://www.bis.org/publ/bcbs122.htm

[7] September 1997, http://www.ebrd.com/pubs/legal/standards.htm

2° Initiatives at the European level

4. At the European level, the present directives contain a certain number of provisions dealing with corporate governance matters. These concern the 2006 directive amending existing directives on financial disclosure, but also the 8th company law directive containing provisions on audit committees, which have been rendered mandatory although states can opt for other equivalent solutions. The directive on take-over bids also deals with certain governance aspects, such as the neutrality rule for the target company, or the rule imposing a mandatory bid upon the acquisition of a 30% or more block of shares in listed companies.

In addition the Community has adopted several recommendations on corporate governance issues, such as the recommendation on director's remuneration[8] (2004) and on directors' independence (2004). Usually the Commission proceeds to an evaluation of the recommendations a certain number of years after their adoption. On the basis of these findings it may decide to proceed to formal Community legislation.

Specific corporate governance measures are also contained in the financial services directives, especially the Banking directive and Markets for financial instruments directive (MiFid).

Apart from these partial initiatives the Commission has stated that it does not intend to propose a European Corporate Governance code, the present laws in the member states still being too diverse.

Recently, the Commission launched a broad investigation on the "one share, one vote" issue: however, this investigation resulted in the finding that there are no fully convincing arguments to introduce a mandatory rule to that effect.

3° Corporate governance guidelines by or for investors

5. Corporate governance behaviour is increasingly influenced by the action of institutional investors, hedge funds, investor voting services and similar activist organisations. Some of these organisations have established very detailed guidelines and model answers to different issues that are likely to come up at general meetings, where these shareholders or organisations are called upon to express their votes. Although the influence of these guidelines is difficult to measure, in at least several instances they have been decisive in shaping the company's action. By way of example, a well know voting services declares always to vote against proposals to introduce dual class shares or other techniques whereby the shareholders' rights may be curtailed. The same applies to the authorisation to issue additional capital without maximum limitation.

The action of Calpers[9] is probably best known among the large public institutional investors in the US. Calpers has published "Core principles of accountable corporate governance" and

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[8] Recommendation 2004/913 of 14 December 2004, OJ L. 385/55 of 29 December 2004.

[9] Calpers or the California Public Employees' Retirement System http://www.calpers.ca.gov/index.jsp?bc=/about/organization/home.xml

"Global principles of accountable corporate governance[10]. On specific items such as rules on director's nomination, specific guidelines have been adopted[11].

A different position is that of Institutional Shareholder Services, a voting agency. Extensive and detailed voting guidelines are published on its website, indicating in which way votes will be cast[12]. ISS has published a "definition of independence" of directors[13], or "director election reforms"[14], and even a corporate performance test for nominated directors"[15]. The relevance of these statements for the corporate suffrage mechanisms but also for shaping the overall corporate governance climate cannot be overestimated.

Euroshareholders is an organisation aiming at protecting investors. It has e.g. published "guidelines on remuneration" [16] and on corporate governance in general[17]. Its Dutch branch has been material in changing the course of action in a number of high profile cases in the Netherlands.

4° National measures within the EU.

6. It would require a Herculean effort[18] to describe the corporate governance regimes in each of the 27 member states. In all states, this regime would in part be based on legal provisions and on voluntary arrangements. Certain provisions of the corporate governance codes may be included in the charter provisions of many companies. Therefore the actual regime is based on a composite of legal sources. Rather than giving an overview of the substantive provisions of the codes it will be attempted here to identify, as far as possible, the legal environment in which these codes have come to light and in which they are being applied.

(a) country overview

7. The corporate governance regimes present a wide variety of approaches and solutions. In some states, preference is given to formal legislation accompanied with additional rules from the market supervisor. In others, codes or recommendations have been adopted, with a varying role for the securities supervisor. In at least two jurisdictions, the securities supervisor has been expressly put in charge of implementing the code.

Some are voluntary in nature and reflect the opinion of some well-intentioned business leaders. The code is generally recommended but without any specific instruments for implementation.

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[10] Calpers: Core principles of accountable corporate governance: http://www.calpers-governance.org/principles/domestic/us/page01.asp; Global principles of accountable corporate governance
http://www.calpers-governance.org/principles/international/global/page01.asp
[11] Calpers on corporate governance: directors nomination
http://www.calpers.ca.gov/eip-docs/investments/policies/equity/corp-gov-dir-nom.pdf
[12] ISS voting guidelines: see http://www.issproxy.com/pdf/2007InternationalSummaryGuidelines.pdf
[13] http://www.issproxy.com/pdf/IndependenceDefintion_CommentPeriod.pdf
[14] http://www.issproxy.com/pdf/DirectorElectionReform_CommentPeriod.pdf
[15] http://www.issproxy.com/pdf/DPpolicy_CommentPeriod.pdf
[16] http://www.veb.net/overveb/es/remuneration.pdf
[17] http://www.veb.net/overveb/es/corpgov.pdf
[18] See P. Mäntysaari, Comparative Corporate Governance, Springer Verlag, Berlin, 2005, 445 p.

Other codes are the product of a national action to establish a common understanding for the local market about good business practice.

8. In the United Kingdom, several Codes have followed one another, the present one being the Combined Code on Corporate Governance 2003[19]. The code states standards of good practice, and listed companies are required to report on how they have applied the standards, and if not, provide an explanation. Pursuant to the Listing conditions, the Code is applicable to all companies incorporated in the UK and listed on the Main market of the London Stock Exchange[20]. The code is monitored by a Corporate Governance Committee functioning within the Financial Reporting Council. This Committee may issue clarifications when significant doubts are raised about the appropriate interpretation of part of the Code. It is not in charge of monitoring the individual disclosures by the companies.

9. According to § 161 of the German Stock Corporation law[21], "the executive board and supervisory board of exchange-listed companies shall declare once a year that the recommendations of the "Government Commission on the German Corporate Governance Code" published by the Federal Ministry of Justice in the official section of the electronic Federal Gazette have been and are being complied with or which of the Code's recommendations are not being applied. The declaration shall be made permanently accessible to stockholders."

The obligation is double: on the one hand the companies have to deliver an annual declaration of acceptance, accessible at the site of the Corporate Governance commission, indicating compliance with the code in general and which provisions have not been complied with. It is not mandatory, although regularly practised in fact, to state the reasons for non compliance.

The Corporate governance commission[22] follows up the application of the code and adopts modifications[23]. It is composed of business leaders, a stock exchange representative and a leading academic.

10. Under Dutch law, art 2:391, para 4 of the Civil code provides that "particular measures can be introduced about the content of the annual report[24]. These measures can relate in particular to a "code of conduct". The Tabaksblat Code[25] has been officially designated as the reference for the Dutch listed companies.
Although a self-regulatory instrument, the code has been established by a committee of leading businesspersons, auditors, shareholder representatives, academics, but with a clear influence from the ministry of economic affairs, as the Netherlands had been confronted with a number of incidents in large Dutch companies

[19] The Combined Code on Corporate Governance, June 2006, http://www.frc.org.uk/documents/pagemanager/frc/Combined%20code%202006%20OCTOBER.pdf
[20] See FSA, Listing Rules, 12.43 A, provides that a company incorporated in the UK must include in its annual report (a) a narrative statement of how it has applied the principles set out in S.1 of the Combined Code, and (b) a statement whether or not it has complied with the Code.
[21] As amended by the Transparency and Disclosure Act, 2002.
[22] So called Cromme Commission, Regierungskommission Deutscher Corporate Governance Kodex, established in 2001 by the Minister of Justice.
[23] The latest version of the code is June 14, 2007.
[24] http://www.cgportal.nl/corpgov.asp
[25] http://www.commissiecorporategovernance.nl/page/downloads/CODE%20DEF%20COMPLEETII.pdf, December 2003

The Code is monitored by a monitoring committee, installed by the minister of finance: the committee publishes detailed findings about the code's implementation by the listed companies[26]. More recently, the attention of the Dutch public opinion has shifted towards the role and position of the shareholders, especially the activist investors[27].

11. In 2004 a Swedish Code on Corporate Governance was published[28]. It was sponsored by a large group of business associations, and the final version drawn up by a Committee appointed by the government. The code is designated as a self regulatory instrument, based on a comply and explain approach and without external monitoring. It applies along with several other self regulatory instruments[29].
The code states that it aims at improving efficiency and competitiveness but also to bolster confidence in the business sector in Sweden and enhancing understanding by foreign investors. As could be expected on the basis of the specific shareholding structure of Swedish companies, rules relating to the functioning of the general meeting and the relations between shareholders, the board and the management receive special attention.

12. Austria adopted a Code on Corporate Governance in November 2002, updated 2006[30]. It is a self-regulatory instrument, using "comply or explain" and is supported by the auditor, financial analysts and asset managers professions. Adherence is voluntary and results in a public declaration of commitment. The code was drawn up by a working party, composed of representatives of industry and academia; it also proceeds to an evaluation of the compliance with the code

13. In Switzerland, the Swiss Exchange has issued in 2002 a Corporate Governance Directive[31], revised in 2006. The Swiss Exchange acts here pursuant to a delegation in the Federal Act on Stock Exchanges and Securities Trading[32] that allows disclosure matters to be delegated to the exchange. It is a self-regulatory instrument, using "comply or explain", except for certain data that must be published[33]. It requires information on shareholder rights, especially on voting restrictions. The directive is enforced by the Exchange's Admissions office and in appeal by the sanctions commission of the Swiss Exchange. This commission has published 8 – anonymous - decisions for violations of the Directive and imposed

[26] Monitoring Commissie Corporate Governance Code. The committee is composed of business leaders, academics with business experience, auditors, a union representative. It is chaired by Prof. Frijns; http://www.commissiecorporategovernance.nl/Information%20in%20English
[27] See the very active discussion about activist investors, private equity investors and hedge funds. Case studies of the main companies can be found in A. de Jong, P. Roosenboom, M. Verbeek and P. Verwijmeren, Hedge Fondsen en Private Equity in Nederland, RSM Erasmus Universiteit, at http://www.rsm.nl/portal/page/portal/RSM2/content_pages/News%20and%20events%20RSM/RSM%20News/RSM%20rapport%20hedgefondsen%20oktober%202007.pdf. The locust have been the subject of attention from the main investor protection association:
Veb 21 sept., 2006 het VEB Sprinkhanenplan, http://www.veb.net/acties/sprinkhanen.pdf
[28] http://www.ericsson.com/ericsson/corpinfo/corp_governance/doc/Swedish_Code_of_Corporate_Governance.pdf
[29] The code mainly refers to several statements by the stock exchanges and by the Securities Council.
[30] http://www.wienerborse.at/corporate/pdf/CorporateGovernanceKodexengl_2.pdf
[31] http://www.swx.com/download/admission/being_public/governance/cg_study_de.pdf
[32] Bundesgesetz 24 March 1995 über die Börsen und den Effektenhandel, and Kotierungsreglement der SWX.
[33] Chapter 5 of the directive, dealing with loans, participations and claims.

disciplinary sanctions (blame). In December 2003, an in-depth review was undertaken for the account of the Exchange of the implementation of this Directive.

Differently from the Directive, which is essentially focused on disclosure, the Swiss Code of Best Practice for Corporate Governance contains a recommendation for good governance inspired by international practice. This code has been drawn up by "economie suisse", a professional body regrouping the core Swiss business world. It is a recommendation, and is essentially not binding.

14. According to the French approach, most corporate governance rules seem to have been introduced in the law[34] or in secondary legislation[35]. The common recommendations of AFEP and Medef [36] do seem to receive some attention. Monitoring takes place by the Autorité des marches financiers[37].

"Aux termes de l'article L. 621-18-3 du code monétaire et financier, les personnes morales faisant appel public à l'épargne sont tenues de rendre publiques les informations relevant des matières mentionnées au dernier alinéa des articles L. 225-37 et L. 225-68 du code de commerce, dans les conditions prévues par le règlement général de l'AMF.

Conformément au dernier alinéa des articles L. 225-37 et L. 225-68 du code de commerce, le président du conseil d'administration ou du conseil de surveillance de toute société anonyme rend compte à l'assemblée générale annuelle des actionnaires, dans un rapport joint au rapport de gestion, des « conditions de préparation et d'organisation des travaux du conseil ainsi que des procédures de contrôle interne mises en place par la société. Le rapport indique en outre les « éventuelles limitations que le conseil d'administration apporte aux pouvoirs du directeur général."

15. In Spain, a new corporate governance code has been in effect since 2005. It was drawn up by a special committee appointed by the government and composed of public officials, business representatives and experts. The purpose was to replace the previous Olivencia and Aldama reports. The code is designated as voluntary, in the sense that companies are expected to abide by the code, and explain where they diverge. However, the code states clearly that there can be no derogation from definitions and concepts, such as "independent directors", a concept that is strictly defined in the code. To be mentioned is the division of the board in

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[34] Art. 621-18-3 of the Code monétaire et financier mandates disclosure of the data referred to in the articles L. 257-37, L. 225-68 and this according to the conditions set out in the AMF's "Règlement general". Said articles refer to the disclosures on "the conditions on preparation and organising the activities of the supervisory board, as well the procedures on internal control introduced by the company, and L. 225-235, dealing with the role of the auditors.

[35] Règlement général de l'AMF, art. 229-9 and Guide d'élaboration des documents de réference: réglementation en vigueur, interprétations et recommandations de l'AMF, 27 January 2006.

[36] December 2003 and a note of the ANSA legal committee, November 2003 are self regulatory instruments supported by AMF; the present amalgamated recommendations consolidate the previous reports Rapport Viénot (1999) and Rapport Bouton "Pour un meilleur gouvernement des enterprises cotées", published by Afep-Agref and Medef, 2002. Both reports were adopted by a group of leading French businessmen.

[37] Rapport 2006 de L'AMF sur le gouvernement d'entreprise et le contrôle interne, 22 January 2007. The AMF stated that « these recommendations and the ANSA legal study throw a very useful light for issuers on the way the president of the company can draw up his report. Therefore the AMF takes due notice of their existence and encourages the issuers to follow their headlines as to the principles and forms of drafting the report of the president, among others with respect to the internal control procedures » (our translation).

three parts: executives, independent directors, and the "proprietary directors" which represent the shareholders. Apart from the code [38] there are supplementary recommendations, several provisions dealing with shareholder relations.

According to art. 116 (5) of the Law on the Mercados de Valores[39]: "Without prejudice to the sanctions that are imposed due to failure to supply the documentation or the corporate governance report, or due to omissions or misleading or incorrect data, it is the National Securities Market Commission's responsibility to monitor the corporate governance regulations, to which end it may gather any necessary information and publish any information it considers to be relevant about the extent of actual compliance."

According to the CNMV[40], the Spanish system is based on two tracks : disclosure is essentially regulated in the law, while the organization and operation of companies is left to the corporate governance recommendations, applying the "comply or explain" rule.

16. Portugal

In Portugal the Corporate Governance recommendations have already been issued by the CMVM, the securities regulator in 1999 updated in 2003, 2005 and September 2007. The recommendations are described as recommendations by and for the market. They contain both substantive and disclosure elements, and apply on a "comply or explain" basis. A regulation of 2000[41], as amended, imposes duties on listed companies to disclose annually a corporate governance report, the content of which is described in the CMVM recommendation. The document calls for information on the functioning of the general meeting and the exercise of voting rights and on the corporate control (Control enhancing mechanisms have to be renewed in the general meeting every 5 years).

The Portuguese Corporate Governance Institute has published a "White book on corporate governance codes and principles" containing numerous recommendations for improvement of actual practices.

17. In Italy, along with the significant changes in the company law, a Corporate Governance code or "Codice di Disciplina" has been adopted - in a renewed version in 2006 - by the Borsa Italiana with support from the Association of Companies Assonime[42]. It is based on "comply or explain". It pays some attention to the role of the shareholders as part of the duties of the board to stimulate the participation of the shareholders. The relationship of the code with Consob, the securities supervisor was modified in the latest revision of the Testo Unico Finanziario: the corporate governance statement will not further be reviewed by Consob as far as the true character of the disclosure is concerned.[43] But on other items Consob will remain in charge e.g. for reviewing the conditions for independence of the board members.

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[38] CNMV Bulletin, Quarter 1, 2007, p. 69.
[39] L Mercados de valores, 24/1988 of 28 July 1988.
[40] CNMV Bulletin, Quarter 1, 2007, p. 69.
[41] Regulation 11/200, 7/2001 and 11/2003.
[42] http://www2.assonime.it:81/assonime/homepage.nsf/corporate_gov
[43] Art. 124ter, TUF. The administrative penalty has also been abolished. Decr. L. 29 December 2006, nr. 303.

18. Belgium

In December 2004 the Belgian corporate governance committee, active within the Belgian employers' association, published a code applicable to Belgian listed companies. As in other states the code is essentially focusing on the functioning of the board and its relationship with management. Some limited attention is paid to the relations with shareholders. The Committee responsible for drawing up the code was composed mainly of leading businessmen, a representative of the stock exchange and one from the securities supervisor. Updating of the code is being considered. Regularly, the application of the code is assessed.
The code is merely voluntary and based on a comply or explain technique. Its application is not supervised by the company's auditors or by the securities supervisor.

(b) The European Directive

19. Directive 2006/46[44] has introduced a formal reference to the corporate governance codes. It states that the annual report of listed companies shall include a corporate governance statement in which reference is made to a corporate governance code. This may be the code that is applicable to that company, or – depending on the national law - the one that it has voluntarily chosen. The statement will contain, on a "comply or explain basis", the derogations from the code, or the items which the company has not applied. Specific items to be mentioned in the statement are "internal control and risk management systems in relation to the financial reporting process" and a series of disclosures relating to the requirements of the directive on take-over bids.

The corporate governance statement shall further contain "all relevant information about the corporate governance practices applied beyond the requirements under national law". One could include among these practices the way the AGM is organised, the operation of the boards and their subcommittees, along with more formal information about the powers of these corporate bodies and the rights of the shareholders.
It will be interesting to notice how the member states will implement this provision.

C. The present stage of corporate governance regulation

1° The codes' genesis and follow up

20. In most European states, there has by now been published at least one corporate governance instrument, in addition to the statutory provisions in the national companies act.
In some jurisdictions, this is referred to as a code, being an elaborate set of provisions, organised in a reasoned way, and aiming at comprehensiveness. Why these documents have

[44] Directive 2006/46/EC of the European Parliament and of the Council of 14 June 2006 amending Council Directives 78/660/EEC on the annual accounts of certain types of companies, 83/349/EEC on consolidated accounts, 86/635/EEC on the annual accounts and consolidated accounts of banks and other financial institutions and 91/674/EEC on the annual accounts and consolidated accounts of insurance undertakings, OJ L 224, 16/08/2006 p. 0001 – 0007; esp. art. 46a of the 4th directive.

been labelled "codes" may require further investigation: there certainly is the will of their draftsmen to confer authority upon an instrument that remains of a self-regulatory nature. There probably was also some mimicry of the Cadbury Code. The Cadbury report contains little information why these recommendations have been labelled "code of best practice".[45]

Some jurisdictions have refrained from using the word "code" and prefer to refer to recommendations[46], others even using "directive"[47]. In Italy it is called "codice di disciplina" although there is no formal disciplinary infrastructure supporting it or sanctioning its violations. In most jurisdictions the code has been labelled as referring to the name of the person who chaired the Committee that has drawn up the code. This usually was a leading businessman, who by allowing his name to be used for referring to the code, has contributed to support the authority of the code[48]. In some cases however, the code is known by reference to the organisation that promoted[49] it, or to a regulator, who chaired the committee[50]. The latter is the case in France, where the different instruments refer to the name of the chairperson leading the drafting committee.

21. A further element concerning the codes' sociology relates to their draftsmen. All codes have been drawn up by committees. However the initiative for making a code was in several cases taken by the stock exchange, or by persons related to the local securities market. This feature illustrates that these codes often have been driven by the need of the market to have a uniform and widely accepted yardstick against which governance practice could be assessed. Institutional investors and voting services often insisted on having a code that could be used for assessing local governance practices.

In other cases the codes originated from the local business association that felt the need to protect the reputation of their markets by professing good governance practice. Critics will add that the intention was also to offer a firmer basis for continuing some of the local practices that were less in line with internationally accepted standards, especially in the field of remuneration, or conflicts of interest.

22. The composition of the committees drafting the codes is also interesting. Some of these committees are composed only of businessmen, other of businessmen and academics, but generally the absence of government officials, or market regulators remains striking. In some of these committees one will find public officials, while in sometimes, the committee was chaired by an official.[51] The dividing line is not the traditional north south division, but should better be seen against the background of the relationship between politics or government and business. If some tension existed at the moment of composing the committee, that may also explain this aspect of the composition of the code, not to mention the content of the code itself. In one or two cases the government itself has installed the committee, where there appeared to be a need for a better structuring governance[52].

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[45] The IMF describes these investigations as ROSCs, referring to different kinds of codes, standards or other soft law instruments.
[46] E.g. France or Portugal.
[47] See the Swiss directive that is part of the listing conditions.
[48] But not so in Switzerland, not in Sweden.
[49] See in Switzerland, the code of "economie suisse"
[50] The "Conthe code" in Spain.
[51] Spain, Sweden.
[52] Sweden, Germany.

The process for drawing up the code usually has followed today's often used method of public consultation. Generally these initiatives have been well received and obviously responded to a need of the markets. This feature explains why the codes are in line with local business practices and concepts (e.g. on the role of block holders).

23. In several countries the codes are being evaluated from time to time. Here a wide variety of cases can be found. In several cases, a private organisation, a university department, or the original drafting committee will draw up tables aimed at checking the points where the code has been followed, and those where responses were weak, or where deviations were explained. These reviews generally do not go beyond noting the number of cases in which the code was formally respected: they are unable to verify the substance of the implementation of the code. In general these committees will also be in charge of updating the code on a regular basis.
In France however, many of the corporate governance provisions have been laid down in the law; it was the securities regulator that established the compliance report[53]. In Germany, where non-compliance has to be reported according to the law, a further analysis is made of the grounds for non-compliance[54].
In the United Kingdom or the Netherlands, the monitoring committee has a wider conception of its role and identifies issues or demands from the business community that should be included in a later revision, or even a change in the legislation. So e.g. does one see in the Netherlands an outspoken concern about the role of the shareholders, especially the more activist ones. Advice is even published as to how companies could deal with this concern[55].

2° As to the substance.

24. The content of these codes show some diversity, due to the differences in the national legal systems. However there are some important common features that will probably be found in all codes. Most of the codes relate first and foremost to the internal functioning of the boards. The provisions they contain are generally of a high level nature, although on some items – director's remuneration e.g. - more detailed rules may be found. They should be considered as self-policing instruments whereby boards impose on themselves a specific structure or conduct. This aspect explains why most codes do not contain elaborate rules on the relationship with shareholders, or their participation in company life, or at least are less explicit and less detailed on this topic. Relations with shareholders are considered outside their scope, also because in times the codes were drafted, shareholder activism was much less prominent than today. Moreover, shareholders could not be bound by a code's provisions: these provisions could only be referred to as "expectations".

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[53] The latest one being: AMF, AMF, rapport 2006 sur le gouvernement d'entreprise et le contrôle interne, January 2007.
[54] See Germany, A. von Werder referred infra nt. 80.
[55] See site of Dutch Corporate Governance Monitoring Commission, containing seven recommendation for assialed companies and nine for the government: http://www.corpgov.nl/page/downloads/Monitoring_Commissie_advies_kabinet_mei_2007.pdf; see: D. Strik, To play or to be in play, over preventie van aandeelhoudersactivisme, Ondernemingsrecht, 2007, 71; comp. Themanummer "Governance codes", Ondernemingsrecht 2007-12, 13 September 2007.

Within the provisions relating to the board's functioning, special attention is drawn to board comitology. Today this would be considered low hanging fruit, but at the time the codes movement started, it was considered avant-garde to require three committees (audit, nomination and remuneration committees) as advisory bodies to the board. The composition of these committees was most of the time explicitly proposed in the codes.

25. More interesting are the subjects that have not been dealt with, or received less attention. The relationship with dominant even controlling shareholders does not receive much attention, although concentrated ownership of shares is the predominant structure on the Continent[56]. Conflicts of interest at board level are addressed by some of the codes, but not at the level of conflicts between board members and shareholders, or between the company and some of its shareholders. Disclosures about methods used to protect control and hence determine the composition of the board are usually not very detailed. Disclosures about the "origin" of the board members and their relationship to one of the dominant shareholders is not always prominently available. Here again one would recognise the influence of the ownership structure in the drawing up of the codes. This is however not a general rule: on the one hand company law may impose sufficient requirements to deal with the issue (e.g. in Germany[57]) while in others ample attention was paid to this issue (e.g. in Italy, or in the Swiss Directive).

D. The relationship of the codes with the legal environment

26. The analysis of the relationship of the corporate governance codes with their legal environment calls for a detailed analysis, as a whole range of issues can be distinguished.

Due to their origin, these codes remain almost always private law initiatives. They do not aim to be recognised as part of the overall legal system, rather to the contrary; they deliberately want to stay outside the reach of the law. However there is a question as to what extent the codes can be kept outside the law in general. This raises the more general question about the extent to which rules can be kept in a legal no-mans land, an issue discussed in the context of gentlemen's agreements.

The legal nature of the codes raises some interesting questions. Are these codes contracts, and in that case on whom are they binding?

Most of the codes have not been conceived as binding contracts. They were the product of a voluntary initiative by persons who themselves are not the addressees of the codes, inviting companies to adhere to the code, whether explicitly or in practice. This may be different for codes that have been developed on behalf of professional or business associations, although here too one should have to verify whether the code has been formally adopted by that association, and whether the association had the capacity to bind its members[58]. In some cases the association may have urged members to sign up to the code. In that case it will become binding on that company, but this again under the proviso that the board accepts to adhere to

[56] Except in Switzerland, where this issue is addressed.
[57] Where most anti takeover protection was abolished by law.
[58] See e.g. Italy and Switzerland, where the codes are association documents but it is not clear whether the member are bound by the association support to the code.

the code. Refusals to abide by the code would at most trigger sanctions at the level of the association.
But even if they are not contracts in the legal sense, they represent "agreements" on good business practice, as this has been defined by the experienced members of the drafting committees. To a certain extent the codes reflect actual practice, but in general they have a sufficient normative value, inviting business to adhere to more credible standards.

27. Codes may also present themselves as self-binding instruments: companies are expected to voluntarily adhere to the code, and declare so in public. Indeed, it is striking how many companies one finds on the internet that present themselves as having adopted the code as a guidance for their governance and explain in great detail the extent to which they are conforming to its provisions. There undoubtedly is a certain public relations exercise behind these announcements, aimed at convincing third parties, especially investors that the company's business is run in a reliable manner and according to best practice. One can presume that these declarations of adherence to the code have been the subject of a formal decision of the board of directors, or at least that they appear to be an act of the company. According to some legislations this adherence should be formalised[59]. But even then, the question arises whether not only the company, but also each of the members of the board, and of the management are bound by the provisions of the code, and whether violations could trigger remedies against them, not only at the internal level – e.g. disciplinary sanction, or labour law sanctions – but also at the request of third parties[60].

As far as the company is concerned, non compliance with the code would normally not call for contractual sanctions, but will be explained by the company under the "comply and explain" principle. If the explanation is not true, or misleading, there might be civil liability or an intervention of the securities supervisors in blatant cases. But even in the absence of any such measure, the reputation of the company may be at stake if its corporate governance policy was unfavourably discussed, or – as happened in several countries – its remuneration policies is being publicly criticized as being overgenerous.

A specific case of self binding is the one in which the code's provisions would have been adopted by the general meeting, since in that case the shareholders could consider the code being part of the contractual relationship with the board, so that violations of the code would be shortcomings in the way the directors have to discharge themselves of their mandate (duty of care). It might also affect the liability of the company towards third parties (i.e. other than shareholders), as gross deficient performance in light of the code's provisions would be attributed to the legal person[61]. Although no clear information is available it does not seem likely that governance codes are frequently adopted in general meetings of shareholders.

28. As mentioned infra, adoption of the code or at least an express reference to it is a regulatory requirement in some jurisdictions. This technique was first introduced in the German companies act, and almost simultaneously also in the Dutch companies law, and will henceforth be the mandatory European standard. A comparable technique is followed in the

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[59] See e.g. in Germany where adherence to the Code has to be published in the official gazette.
[60] This is a matter of national company law. In most cases, there would be no liability except if the violation amounts, independently of the code provision, to gross negligence.
[61] And might give right to action for even smaller shareholders. According to the Dutch companies act, art. 224a, shareholders with 1% have the right to call a general meeting. Moreover the judicial intervention of the Enterprise Chamber can be triggered by a motion submitted to that jurisdiction by 10% shareholders.

French law, where the law provides that the chairman of the board reports to the general meeting of shareholders about the "conditions of preparation and organisation of the board activities as well as on the internal control procedures as introduced by the company. It should indicate the limitations that the board has imposed on the powers of the director general"[62].

A next step on the legal ladder would be that compliance with the code has become part of the conditions to access the regulated market[63]. It will then normally be a condition for staying registered on that market, although non compliance will be difficult to sanction as removal of the shares from the market will rather prejudice the investors and less the company. Here the governance document would be imposed by unilateral act, being a decision of the stock exchange acting upon its delegated authority. Whether the acceptance of the listing conditions is to be qualified as a contract depends on the national legal system: with the privatisation of the stock exchanges listing conditions are part of the private law arrangements between the issuer and the stock exchange, and violations could result in private law sanctions, including conventional penalties. In some jurisdictions, some provisions may even have been laid down in the secondary law[64].

29. Adherence to the code may also be part of the lending conditions imposed by credit institutions: loan conditions may require certain guarantees in governance terms, especially if a particular shareholder would heavily dominate the debtor. The position of the credit rating agencies is different as they do not impose conditions but merely take this element into account in deciding on their ratings. Indirectly however, their influence on governance in general will be considerable, whether through their usual credit ratings or as a consequence of their new business in corporate governance ratings.

The ultimate case is the one in which the corporate governance provisions have been largely introduced in the law. In all jurisdictions, some governance provisions of course are part of the law, but here one refers to the case – more specifically France – where the voluntary regulation has obviously lost most of its significance for being superseded by statutory provisions.

E. The moving relationship between the codes and company law

30. The corporate governance codes function within the boundaries of the freedom left by the legal system, especially by the rules on company law. Codes could not go against company law rules or provisions, but can merely complement the law on matters that have been left blank in the law. This is e.g. the case on the rules on board decision making that have not been detailed in most companies acts. The same applies to rules on the composition of the board, although here one sees more and more laws that mandate independent directors. Matters that the companies acts have not touched upon, for political or other reasons, were first regulated in the governance codes, such as the requirement to have an audit committee – obviously still controversial[65]- or the matter of disclosure of remunerations[66], in some states a hotly debated issue. The surface of this free zone that can be occupied by self-regulation, will depend on the applicable national law. But in general, one could state that matters such as the

[62] L. 235-37 and 235-68, last paragraph.
[63] See the Directive of the Swiss Exchange, supra nr. 13.
[64] E.g. in the French system, where art. 621-18-3 du code monétaire et financier refers to the Règlement de l' AMF.
[65] See art. 41, 8th directive 2006/43 of 17 May 2006, OJ L.157, 9 June 2006, 87.
[66] Mandatory disclosure in the Netherlands and in France.

internal functioning of the board, the techniques to introduce sufficient checks and balances in the boards' composition, the duties and privileges of board members, the organisation of internal committees of the board and their composition, their remit, the organisation of internal controls, the relationship between board and management, are matters that usually cannot be detailed in statutory provisions and are better dealt with in a self regulatory instrument, on a comply or explain basis. Here the codes typically act as principle-based instruments by stating the outcomes and leaving the actors wide freedom to give a specific form to the objective formulated in the code. On other matters, codes have attempted to set the tune, and can be considered as the vanguard of legislative action, triggering considerable interest from the parliamentarians, who generally dislike laws outside their reach.

Matters of sanctioning are for obvious reasons, not included in the usual codes. But alternative sanctioning mechanisms may be in place, based on associative rules, or contractual provisions.

31. Some corporate governance codes are composed of a mixture of company law provisions and self regulatory recommendations. This is more clearly the case in the new EU member states where codes were generally developed by the stock exchanges, but also have had a certain a pedagogic function[67]. It goes without saying that this is a mere matter of presentation without any influence on the substance.

32. When corporate governance provisions are under consideration, there always is a discussion whether that should be done by self-regulatory instrument, or by statutory provision. The business world pleads for flexibility and the need to adapt to the individual cases, while the political world usually wants stricter rules for which the existing enforcement instruments can be put at work.
In fact the discussion is usually more complex: although a wide agreement exists with respect to the need to follow a principles based approach, there will be specific sensitivities depending on the identity of the members of the Corporate Governance Committee. So e.g. can one expect the representative of the stock exchange to adopt a stricter position as the reputation of his firm is at stake, although by being too strict he may scare off candidates for listing. Representatives of industry will be more sensitive to issues such as management remuneration, although their attitude may be considerably different depending on the size of the company in which they are involved, or on its pre-existing listings on foreign exchanges, including American markets. If the latter is the case, their sensitivity to additional requirements that go into the direction of Sarbanes-Oxley will logically be less intense.

The draftsmen of the code will also be confronted with the attitude of the ministries in charge of company law, usually the Ministry of Justice. Sometimes some tension with the Ministry of Finance, who is in charge of stock exchange matters, may flavour the discussion. The ministry will often plead for reserving the largest number of subjects for legislative action, even if the latter may not intervene in the short time. Coordination between the two is essential and should avoid that overlapping initiatives are taken. The role of the corporate governance codes is not to enact laws, but to offer guidance for company bodies and their members, day-to-day management of the boards in terms that are usually unfit for state legislation, with its rigidity and its complex rules of sanctioning. If there has been a certain

[67] See for an overview: EBRD, Strengthening corporate governance practices, Law in Transition, 2006, at 64-65. In the Czech and Slovak Republic and in Lithuania, the securities regulators were closely involved in the drafting of the codes.

competition between the two work streams, obviously the drafting committees have been able to map the limits of their task, without upsetting the public authorities. But this remains a fragile equilibrium: if the results achieved by self regulatory efforts appear not to be satisfactory in the eyes of the politicians and the public opinion, one can expect legislative intervention to be tried. This has been the case especially with respect to the subject of remuneration of directors and managers.

33. The tension between state en self-regulation illustrates another aspect of the code movement, it is that codes have often been seen as instruments to avoid a legislative intervention. Several elements have played a role here: codes are more flexible and – due to the expertise of their draftsmen – are addressing the subject matter more adequately, while the “comply and explain” approach allows scalability and proportionality, needed for the wide range of company profiles on the European markets. Moreover, the sanctions that would attach to violations of a statutory provisions would be so far going including significant financial risks due to the liability regime in many states – less severe for violation of private contract provisions - that draftsmen and legislators alike rightly considered it better to leave the matter to self-regulation.

The dividing line between state regulation and self-regulation will always remain unclear, controversial and shifting over time. It will be a matter of national choice to determine whether more reliance is put on the one over the other. France, after having first tried a self-regulation approach, has obviously chosen for the more state based system. But in other jurisdictions, a certain balance seems to have been reached, and maintained.

F. Enforcing Corporate Governance Codes

34. As almost all existing corporate governance codes are of a non-statutory nature, their binding force cannot be based on the usual legal techniques for enforcing the law, i.e. liabilities, injunctions, fines, imprisonment, or any other coercive technique found in national law. Generally soft law rules have to rely on the voluntary behaviour of their addressees. Although voluntary in essence, this does not mean that there are no strong incentives for companies to comply with the codes. The sanctions will then essentially be economical or financial, not legal. To what extent these incentives will suffice to ensure substantive implementation of the codes is often doubted, but difficult to affirm or deny for lack of strong empirical data. At present in many jurisdictions there are very sophisticated data about the formal implementation of the code’s provisions, e.g. by indicating how many companies have designated independent directors, of have appointed audit committees[68]. Whether these directors are effectively independent, or whether the audit committee adequately performs the tasks that it is expected to perform, is much more difficult to verify. This is the debate between “formal” and “substantive” implementation of the codes. The debate has taken a political turn: in some states, the legislator has intervened by requiring that at least formal adoption of the code should be ensured, while introducing flexibility by allowing “comply or explain”. In other jurisdictions, there has been a discussion whether the securities supervisor

[68] See von Werder for Germany, nt. 80; Assonime for Italy, nt. 81. Deminor, a consultancy firm specialised in the protection of minority shareholders, also has established comparative tables covering several European jurisdiction: see e.g. the study on he application of the one share - one vote principle in Europe, March 2005.

should not be involved[69]. In only two jurisdictions, the securities commission has been expressly mandated to check compliance with the code[70].

The effectiveness of the present monitoring techniques is sometimes put in doubt: the explanations given for non compliance are according to these critics, far from convincing, and there are no remedies if no explanation is given. Monitoring by the market or by the investors is considered too weak, as investors do not show to have a strong interest in these matters.

35. There are numerous instruments and techniques that support the voluntary implementation of corporate governance rules. Most of these create incentives for companies to abide by the codes' provisions. Market pressure and the fear of reputation damage will often suffice for business leaders to adhere to the code. But some of these techniques present a harder face: although not part of the law as such, corporate governance codes do not function in a legal vacuum: the relationship with the existing legal system should be clarified. Finally, in some states, a formal link with the companies act has been introduced. This has also raised the question to what extent these obligations can be supervised by the securities supervisors.
One could distinguish between enforcement by the law and enforcement by the markets[71].

1. Market guided enforcement

36. Under this heading, a certain number of techniques are regrouped that create incentives for implementing the code. They have in common that these are not legal instruments while their effectiveness may greatly vary with the specific circumstances in which they are put to work. A director's concern for his reputation e.g. may differ considerably not only from state to state, but also over time. Many of the techniques are put to work simultaneously, but not necessarily in all given cases.

37. One of the strongest enforcement devices is the appreciation of the external world of a company' governance. This is enforcement by the market and underlines the importance of the disclosure obligation, whether of the formal "governance statement" or of other any other disclosures that are relevant from a governance point of view. By imposing disclosure, the codes expose the company and its board to justification, outside criticism and most importantly, to market evaluation. In general, board members can be expected to protect their reputation capital and will voluntary adhere to good governance practices, even in the absence of formal codes. The media have become more alert to these issues and regularly expose blatant shortcomings. Pressure from the peers should not be underestimated, as weak governance practices on one board may spill over to damage the reputation of other boards. But more important is the pressure of the "markets", this notion to be understood here in the broad sense, including all actors intervening in the capital markets: regulated securities markets, rating agencies, investment bankers, specialised governance organisations, activist investors and their advisors, the media, the public opinion and so on[72]. The most direct effect will be on the company's rating: rating agencies are now including governance in their rating criteria, while developing specialised ratings specifically addressing a company's governance.

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[69] For details see the discussion in the Dutch Parliament, described in E. Wymeersch, "The Enforcement of Corporate Governance Codes", in: *Journal of Corporate Law Studies*; April 2006, 113-138, ssrn 7593764 2006.

[70] As seems to be the case in Spain.

[71] See the paper by the undersigned: "Standardisation by law and markets especially in financial services", to be published.

[72] This is the case for the Italian, French, Belgian, Swedish and Swiss codes.

Investment bankers in charge of placing securities, but also candidate directors may take a close look at the governance, while consultants and lawyers in general will advocate compliance with the applicable governance code. These professional parties will not bet their highly valued reputation on deficient governance of a company they are professionally or financially engaged in.

More specific market linked enforcement instruments originate from the stock exchanges and from external monitoring firms.

- Large investors

38. Among monitoring investors, institutional investors should especially be mentioned, as often they are obliged by law to vote at the general meeting and hence take a public stand on governance issues. They will hesitate to acquire shares in issuers whose practices do not abide by usual governance standards[73]. When these issues are voted on – e.g. introducing a poison pill, or other techniques allowing management to entrench itself- these investors will generally instruct a proxy organisation to vote against the proposals[74]. Voting organisations practice standard conditions for dealing with specific governance issues – e.g. on multiple voting rights - and these may flow through to the governance codes themselves.

Special attention should be paid to some important institutional investors that have stated firm governance policies and implement these in their action plan v.à.v. companies they have or plan to invest in. Calpers, a Californian pension fund, the most salient example[75]. But other institutional investors, although not developing own governance activist programmes may link up with activist investors and so significantly influence the future of the company[76].

Hedge funds and similar activists shareholders are increasingly engaged in exercising pressure on companies, the governance of which they consider unsatisfactory. By demanding governance improvement they expect the market price to increase. Sometimes their action goes much further and extends to requesting fundamental changes in the company structure, and even its split up[77]. Activist shareholders and voting agencies have undoubtedly had a significant influence on governance practices in many European companies, in some cases resulting in dramatic governance changes (e.g. Royal Dutch having abandoned its bi-national structure under pressure from its shareholders). Some hedge funds specialise in investments in companies with the aim of improving the governance, what would normally result in a positive return on the shares.

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[73] See specifically about the attitude of the institutional investors with respect to the "one share, one vote" issue: ISS, Report on the Proportionality in the European Union, 7 April 2007, http://www.ecgi.org/publications/documents/report_en.pdf

[74] See ISS voting instructions : http://www.issproxy.com/pdf/votingservices.pdf

[75] See Calpers, 2007 Corporate Governance Focus List at http://www.calpers.ca.gov/index.jsp?bc=/about/press/news/invest-corp/focuslist.xml

[76] See e.g. in the Stork case, Ondernemingskamer, AZ6440, 17 January 2007, for an English summary, see http://www.houthoff.com/en-gb/content.aspx?cid=3774&mid=3&aid=164

[77] See OECD report, The implications of Alternative Investment vehicles for corporate governance. A synthesis research about Private Equity Firms and "Activist hedge funds", 20 March 2007.

- Interest of the Stock Exchanges

39. Often corporate governance codes are linked to stock exchanges: the exchange has a clear interest that the companies it has admitted for trading are complying with good governance standards and hence deserve a high quality label. Therefore corporate governance initiatives often originated from stock exchanges, while governance conditions are often found in listing rules[78]. Upon access the exchange will usually be able to enforce its rules. To maintain abidance to the rules, or to impose them on already listed companies will be more difficult. Apart from "name and shame" the exchange could delist its shares. In practice delisting is not an option due to the damage that it may inflict investors. Therefore some exchanges follow a softer approach and motivate companies to adhere to its code. Some even organise education and training of directors and investors relation specialists[79]. Here the carrot will win over the stick.

- External Monitoring

40. External monitoring may document the degree of implementation by the listed companies taken as a group. Reports on monitoring illustrate good practice and will stimulate other companies to adopt similar conduct. Here again peer pressure and pressure from the media will be important. This monitoring is sometimes done spontaneously e.g. by academics[80], by associations of listed companies[81], by consultancy firms[82], the stock exchange[83] or more exceptionally by the securities supervisor[84]. In a couple of cases, the monitoring committee

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[78] This is the case with the Governance Code of the Budapest Stock Exchange, 2004, with the Slovak Corporate Governance Code of 18 March 2004. The UK case is different as the Governance Codes are part of the listing conditions. Previously, these include important governance rules dealing e.g. with significant and controlling shareholders – their influence being limited to 30% – and to conflicts of interest. With the transfer of the self regulatory rules to the UK Listing Authority, as exercised by the FSA, these provisions have obviously been dropped.

[79] This aspect is mentioned in the Polish Code.

[80] A. von Werder, "Kodex Report 2005: Die Akkeptanz der Empfehlungen und Anregungen des Deutschen Corporate Governance Kodex", Der Betrieb, 2005, 841, reporting annually on the implementation of the German Code by listed companies and illustrating the continuous adaptation of issuers to the new standards.

[81] Assonime, Analisi delle stato di attuazione del Codice di Autodisciplina delle società quotate (Anno 2005), study nr. 25, December; Analisi http://www1.assonime.it/assonime/corpgov/ca.nsf/103/FCCA0E45ABAFE5BDC12572900050ED29/$File/FINALE_+26_febbr_analisi+2006.pdf?OpenElement2005 ; http://www2.assonime.it:81/assonime/homepage.nsf/corporate_gov

[82] Deminor, "Good corporate governance pays off", http://www.deminor.be/download.do?doc=deminorratingDocs/Rob_Bauer_Study-English-030425.pdf; Heidrick & Struggles, 10th Annual Corporate Board Effectiveness Study, 2006-2007 http://www.heidrick.com/IC/Published/Governance/ and the 2007 Raising the Bar, Corporate Governance in Europe 2007 Report.

[83] OMX, the stock exchange in Finland monitors the Finnish Code.

[84] For France: Rapport de l'AMF sur le gouvernement d'entreprise et les procedures de contrôle interne, 13 January 2005, Revue AMF, January 2005; see the website of the Belgian Banking, Finance and Insurance Commission, published detailed studies on aspects of disclosure including elements of governance: http://www.cbfa.be/fr/gv/info/circ/pdf/fmi_2003_02.pdf#open. On the Code: see VBO website: http://www.corporategovernancecommittee.be/nl/commissie/samenstelling/default.aspx. The Polish securities supervisors takes a strong interest in the compliance, requiring companies not only to

was the direct continuation of the committee that drew up the governance rules[85]. The role of these committees is not to verify the individual compliance by individual companies, but to screen the overall practice in a given jurisdiction. The committee would be able to publish its assessment, usually anonymously. It could also recommend changes to the code. This type of monitoring committee has been introduced in the Netherlands, in Switzerland and in a different form in the UK[86]. One may wonder whether a monitoring committee could use the "name and share" technique with respect to companies that refuse to give in to its orders to comply with the code. The rules on libel or slander would most of the time prevent this approach. Official review panels could take a stronger stand, as the law would authorise them to publish the names of the recalcitrant companies. A short overview of the result of some of the reviews will be dealt with under the heading of the effectiveness of the codes.

Little analysis has been undertaken on the use of governance criteria in connection with loan conditions. Sometimes the loan documentation will contain explicit clauses that can be classified under the governance heading, such as the need to have a sufficient number of independent directors on the board, or the requirement for a formal audit committee. Well known are conditions on the change of control, as this may lead to accelerating the loan. Also state contracts, or subsidies may be made contingent upon respecting a certain number of good governance rules. One could imagine that large creditors would be interested to know that the company is run according to the prevailing governance concepts and more specifically in accordance with the applicable code. These covenants may therefore be considered as another monitoring device.

2° Empirical studies on performance

41. If corporate governance measures and disclosures have a beneficial effect on the companies that have put them to work, this should appear from empirical research investigating the relationship between governance actions or provisions and market return. Theoretically the firms with the strongest corporate governance practices should show a higher return than those with weak or even deficient governance. This subject has been investigated by numerous empirical studies, essentially in the US but also in Europe, that have tried different methodologies to establish a relationship with performance. There is of course an academic debate about methodology and about the factors that have to be compared: stock prices, firm performance, about the relevant corporate governance facts or measures to take into account, etc. The risk of endogeneity is considerable. But the overall outcome remains unclear: there appears to be no clear evidence of an indisputable overall positive effect of governance disclosures and practices on market returns in general although specific measures

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explain non compliance, but also when hey will comply, making the code almost mandatory. The Warsaw Stock Exchange alos threatened sanction for on compliance.

[85] See the Dutch Frijns Committee, http://www.commissiecorporategovernance.nl/home.html the commission was installed by government decision. See infra nr. 48. The Swedish Corporate Governance Committee also undertakes monitoring, following a quantitative approach.

[86] The Financial Reporting Council, an independent regulator for corporate reporting and governance, created from 1 April 2004 is in charge of setting, monitoring and enforcing accounting and auditing standards. It task has been widened to the promotion of high corporate governance. standards by monitoring and maintaining the Combined Code and associated guidance. It tests the code on its effectiveness, gives interpretations, and prepares revisions of the code. Detailed analysis of compliance is contracted to an auditing firm. The FRC acts without explicit statutory base, although reference is made to the rules on listing on the exchange, which require compliance with the Code.

show a stronger correlation. Some studies, especially from the consultancy side[87], consider that the effect of "good governance" is substantial.

A first series of studies investigated the relationship with specific events, or specific corporate governance rules such as the proportion of outside directors[88], or with board committee structure[89], or board size[90]. Only a small fraction of governance provisions shows a relationship to firm valuation[91] while others conclude to the absence of any relationship[92]. But other studies revealed a modest [93] or even a significant[94] relationship with performance.

42. This mixed observation was further detailed in a recent large investigation by Brown and Caylor[95] who reviewed a population of 1757 US firms on the basis of 51 governance criteria. They concluded that poorly governed firms have a lower return on equity and lower returns on assets, and conversely that there was a significant positive association between corporate governance practices and operating performance both in terms of ROE and of ROA. The vast majority of corporate governance mandated individual measures however are not linked to firm profitability. Looking into more detail at specific governance provisions, of which they selected 51, they found that most governance provision mandated by Congress or by the Stock Exchanges were not significantly and positively related to operating performance. Two selected Sarbanes Oxley provisions appeared to have a stronger relationship to operating performance: namely that auditors' consulting fees should be less than their audit fees and

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[87] A positive correlation was stated by P. Coombes and M. Watson, "Three surveys on corporate governance", McKinsey Quarterly, 4/2000 and to Pricewaterhouse, Shareholder value and corporate governance 1997 but these studies have no strict scientific aspiration. However, R. Romano made a large investigation of the effect of the Sarbanes-Oxley Act and concluded that most measures imposed by SOX did not have a material effect on the firm's returns, and some even a negative impact: See Romano, "The Sarbanes-Oxley Act and the Making of Quack Corporate Governance", SSRN.com/abstract=596101.

[88] Bhagat and B. Black, "Relational Investment and Firm Performance", 2002, ssrn 330100, found no relations between the proportion of outsider directors and ROA or assets turnover. But Black, Jung and Kim, "Does Corporate Governance affect firm value? Evidence from Korea", ssrn 311275 found a strong relationship.

[89] A. Klein, "Firm performance and board committee structure", (98) 41 J. Law Economics, 275 found no relations between board independence and operating performance but a significant relations with insiders' presence on the board and the existence of investment committees.

[90] D. Yermack, 1966 found an inverse relationship between board size and profitability.

[91] Bebchuk, Cohen and Farrell, "The costs of Entrenched Boards", (2005) J.Fin Econom, 78, 409-433.

[92] Gompers, Ishii, Metrick, "Corporate Governance and Equity Prices", 2003, ssrn278920; no finding that better governed firms have a higher return on equity. This was contradicted by Core, Guay and Rusticus: Does weak governance cause Weak Stock Returns? 2005, ssrn, 533582 who used other parameters.

[93] Larcker, Richardson and Tuna: "How important is Corporate Governance", (2005), ssrn, 595821.

[94] Ashbaugh, Collins and LaFond: "Corporate Governance and the cost of Equity Capital" (2004) ssrn, 639681; Enrique Fernández-Rodríguez, Silvia Gómez-Ansón, Álvaro Cuervo-García: "The Stock Market Reaction to the Introduction of Best Practices Codes by Spanish Firms, Corporate Governance, An International review", vol. 12, 29-45 (2004) Renato Grandmont, Gavin Grant, Flavia Silva, Deutsche Bank Research : Beyond the numbers: corporate governance implications for investors (2004).

Relationship with the cost of capital ; Doidge, Karolyi and Stulz, "Why do countries matter so much for Corporate Governance", 2005, 580883, NBER, fall 2005: Access to global capital markets sharpen firm incentives for better governance;

72 L.Brown and M. Caylor, "Corporate Governance and Firm Operating Performance", December 2005, ssrn 754484.

that audit committees should consist solely of independent directors. But they found significant positive relationship to operating performance for two other stock exchange mandated provisions, i.e. that both nomination committees and remuneration committees should be composed of independent directors only. In both cases, freedom from management's influence and willingness to link pay to performance were remunerated by investors. Also eight other provisions showed positive and significant relations to performance but none of these were Sarbanes Oxley or NYSE mandated. Obviously their selection of provisions took place on political grounds, without regard to operating performance. The more strikingly relevant ones were: "it is not authorized to issue blank check preferred stock" (entrenchment instrument)"and "non-employees do not participate in firm pension plans" (conflict of interest issue); also: "at least one director participated in an ISS accredited director education programme". Interesting among the more sensitive factors are statements like: no former CEO on the board, or companies should expense options, where options should on average be less than 3% over the last three years. Most other provisions chosen were found to be neutral.

To conclude: to determine a strict relationship with corporate governance codes and firm performance is still a way off. One can safely estimate that weak or bad governance practices will have a negative effect on he company's share price, but it seems controversial to state that the opposite is true. However, individual measures may have a value enhancing effect. It would be useful if similar empirical studies were undertaken on a larger scale in Europe taking into account governance codes and provisions that are typical for European companies.

2° Legal sanctions and remedies

43. Apart from market sanctions, can corporate governance codes be enforced by law, or more generally are they legally relevant?[96] Here again different aspects should be distinguished. First one should establish who is involved in the adoption process of the code within the company. Secondly what liabilities or other sanctions could be attached to whether the absence of any respect for any code, or for particular shortcomings.

The starting point is the initial responsibility of the board of directors to ensure that – within the applicable legal framework - the company's corporate governance is well balanced and in accordance with the applicable code. In a two-tier corporate structure, this task should be taken up by the supervisory board. Hence the board should be paying sufficient attention to its own functioning, to board attendance, look into the contribution of each of its members, and to evaluate its governance from time to time. Mechanisms should be introduced that ensure these objectives, e.g. by organising induction procedures, proceeding to self assessment, appointing a separate corporate governance assessment committee within the board or call on external expertise.

The board should report on its governance and the attention it has paid to it. This is the "governance statement", that will become mandatory according to the European Directive.[97] Disclosing the report brings with it external responsibility, whether to the shareholders, or to the markets in general: apart from reputation risk, directors may become liable towards the

[96] See Bühler, Corporate Governance und Compliance, Modewörter oder Bedürfnis im schweizerischen Aktienrecht, FS Forstmoser, 211-225.
[97] See supra nr. 19.

company and towards third parties if the statement contains untrue facts, or is likely to mislead them. And it may – depending on the national law - trigger the intervention of the securities supervisor, as the latter is in charge of the surveillance of most of the disclosures made by the company[98].

44. To what extent shareholders should be involved in this process differs considerably: in most codes, they are informed about the governance statement, but do not approve of it, at least not formally[99]. In two tier board systems, the supervisory board – but not the general meeting – usually approves of the statement. With respect to certain items, e.g. the designation of an independent director, the shareholders would be more directly involved: his election by the general meeting would give credibility to his qualification as an independent director[100]. But stronger involvement of the shareholders will usually be considered interference in the functioning of the board, and hence be incompatible with the structural model of the company.
Companies are not run by shareholders: if they are not satisfied, they should dismiss the board, and appoint new directors.

Very exceptionally shareholders may have some say in developing specific governance decisions, i.e. in cases where some of the governance rules would be laid down in the articles of incorporation. In public companies, this is seldom if ever the case. Although no cases are known, boards have a general responsibility for the quality of the governance statement and may be dismissed if the statement – differently from the actual governance practices - is deemed utterly unsatisfactory by the general meeting, as this may have a negative influence on the share price. Cases are know where under the influence of activist shareholders, board were forced to leave, and more specifically where the CEO has to leave, usually triggering a share price increase[101].

Should the auditor not be involved in verifying the corporate governance statement? In many jurisdictions he is an organ of the company and has intimate knowledge of its functioning. The responses found in the comparative analysis vary considerably: in some states his intervention is considered part of the verification process leading to the annual accounts and the annual report. In others it is stated that he should limit himself to verifying the figures that are mentioned in the report. But in any case, his intervention can only cover whether in accordance with the provisions of the code the required disclosures are made, but not whether the information is true or accurate. Here too, his intervention is merely formal, and does not cover substance[102].

98 Mostly by virtue of the national laws; the Transparency directive, 2004/109 of 15 December 2004, OJ, L 390, 31 December 2004, 38, however does not contain an express reference to this information, as it may not be part of the “annual financial report” report. Hence it would not come within the ambit of the supervision exercised by virtue of the Transparency directive, but the national law could state otherwise.
99 If it is part of the annual report, the approval of the latter would cover the corporate governance statement. One could discuss whether this approval includes agreement with the exposed governance statement.
100 See the criteria for independence established by the institutional investors associations, or the voting agencies, nt. 5 and the accompanying notes.
101 See the data by Julian Frank.
102 For further details, see Wymeersch, nt. 57.

45. Once the code has been formally adopted at board level, it will have to be considered part of the internal rules of the board, and therefore could be invoked by board members against their colleagues. Although there is no clear perception by board members this is to be the case, there would be no difference with internal rules – "by laws" - of the board as exist in many companies. Even in legal proceedings among board members, or against the board, the code's provisions may become legally relevant, as being part of the contractual framework that supplements the company's charter.

To have an effect on shareholders, the code's provisions would have to be considered part of a contract in favour of third parties [103] as they could be invoked by the shareholders[104], even without the code having been formally submitted to the general meeting. If the code would impose certain rules or obligations on the shareholder in general, these would have to be approved by the AGM. For instance, rules on calling a general meeting by individual shareholders, on putting issues on the agenda, submitting questions to the board or obtaining answers to the questions posed by a shareholder often are part of the codes, and could become legally relevant for shareholders – even if they have not been approved by the general meeting as giving an individual right of action to the shareholders[105]. Nothing prevents a board from obliging itself e.g. to call an AGM at a lower percentage than the one provided in the law, and the shareholder could hold him to that promise.

46. The code could also be legally relevant in legal actions against directors in liability whether for neglecting their duty of care – or the extent that the code contains more severe provisions on conflicts of interest- for violation of their duty of loyalty as well, in the context of actions by individual shareholders - or by the board, provisions of the code may be considered as binding on that director, as he has accepted, in a public statement adopted by all directors, to abide by it. Even outside this context courts may find the code offering a useful source of information about the how to interpret the duties of directors. A reference to a code in a judicial decision – even sometimes relating to unlisted companies - would correspond to the well known phenomenon of the court filling in the blanks left in the legal system by seeking inspiration in public statements drawn up by specialists and standing for widely accepted quality standards and good business practice. Here we meet the more general phenomenon of the use of soft law rules for giving content to generally framed legal obligations.

Corporate governance rules in general have up to now rarely been discussed in courts[106].

46. Directly linked to the previous question is that of the legal sanctions against companies that refuse to adhere or to implement a code which they voluntarily subscribed to.
In the case of a refusal of adherence in cases where the law prescribes so - especially relevant after the implementation of the European directive - the sanctions applicable according to national company law will apply. If acceptance of the code has been mandated by the law, this refusal to designate a code as the binding standard would be a violation of the law, that may expose board members to liability, apart from administrative or criminal sanctions, if

[103] Comp. "stipulation pour autrui", "Verträge zugunsten Dritter", § 328 BGB.
[104] E.g. "Verträge mit Schutzwirkung zugunsten Dritter".
[105] Provided of course that they are not contrary to the companies act or to the companies charter.
[106] See Dutch case HR 21 February 2003, NJ, 2003, 192, nt Ma (HBG case) where the Court considered that the obligation to consult shareholders in support of the company's decision on a takeover or other private reorganization "has no legal basis in present law, nor in views accepted on corporate governance in the Netherlands".

any. Third parties that would have been harmed might sue in damages, but it is likely these will be very hard to prove.

G. Are corporate governance codes effective and effectively applied ?

47. As many corporate governance codes are fully voluntary, often being based on a "comply or explain" technique, one can wonder to what extent corporate governance codes can be considered an effective mechanism to guide corporate conduct, and related to this question whether they are more effective than legislation. This question should be distinguished from the previously discussed item whether corporate governance rules in general have a beneficial effect on the companies, and more particularly on their market returns.

The question is not easy to solve[107]. On the one hand there are extensive assessment reports about compliance with the corporate governance code provisions, in almost all jurisdictions. These reports indicate the provisions which companies have complied with in the sense that they have given some information or indicated why they did not comply. The reports however, do most of the time not contain information about the substance of the disclosures and the extent to which the companies have effectively adhered to the intentions or the philosophy of the code. Whatever its formal character one should presume that the information disclosed in the corporate governance statement adequately reflects the applicable code's provisions[108].

Are self-regulatory corporate governance codes better implemented that comparable state laws?
In comparison with the well-documented status of formal compliance with the voluntary codes, one has much less information as to compliance with the statutory provisions. An analysis would require a systematic review of the case law – both civil and criminal – which is not available in any jurisdiction, and one may doubt whether that would yield a satisfactory insight in the matter. As far as criminal enforcement is concerned one can state that in most jurisdictions prosecution for violations of provisions of a more technical nature is usually very weak, unless these are part of an investigation in more serious misconduct (fraud, embezzlement and the like).

48. In many jurisdictions, tables about the enforcement of the code provisions have been drawn up. As mentioned above, these are usually private initiatives. A few data can give a more precise view of these assessments.

Netherlands

The implementation of the Netherlands Tabaksblat Code by the 146 listed companies reveals a high implementation degree (92%) with 4% choosing the explain option[109]. The explanation was judged "understandable" in 85% of the cases, but negative for 12%. The weakest points related to disclosure of remuneration (73% disclosed, 6% explained); the independence of

[107] See C. Jungmann, "The effectiveness of corporate governance in One-Tier and Two-Tier Board Systems, Evidence from the UK and Germany", ECFR, 2006, 426-472.
[108] Significantly, in the Belgian assessment, it is mentioned that unless the company indicates otherwise the code provisions are presumed to have been complied with.
[109] Netherlands,
http://www.commissiecorporategovernance.nl/page/downloads/14087_NL_Rapportage1.pdf

board members (86% and 9% explanations) and the organisation of the internal audit function (83% implemented, 17% with explanation). In large companies best practice provisions were rather less frequently implemented when these related to the report of the remuneration committee, the contract clauses with managing directors and the strategic discussion in the supervisory board. Striking is the importance paid to the relations with shareholders, especially the approach that could be followed for dealing with aggressive shareholders[110].

Belgium

On the basis of data from 135 listed companies, an annual review is undertaken by the Institute of directors and the Employers' Association[111]. It mentions that almost all large listed companies have published a corporate governance charter. The compliance rate was 79,7% for all companies (87% for the largest ones) while the explain option was used by 5,1% (4,7% for the largest companies). Compliance was weaker with smaller companies, especially those with a free float of less than 30% of shares issued. Items that particularly called attention where the 5% recommended threshold for calling a general meeting (where the law provides for 20%), the policy relating to conflicts of interest, rules on hiring and firing and rules of management stock options. Incomplete information relating to remunerations[112], and to the frequency of the meetings of remuneration and nominations committees were also mentioned.

United Kingdom

The Financial Reporting Council regularly reviews the Combined Code 2002[113]. However the methodology is different in that it consults the market on a number of questions that are dealing with the overall assessment of the code's functioning rather than with the individual items in the code. This inquiry reveals that respondents were worried about "box ticking" and "boiler-plate" disclosures. Also the Council supports the dialogue between boards and their shareholders, and considered changes in the voting procedures.

Italy

The Codice di disciplina is assessed every year by the Association of Italian companies limited[114] and the Association of issuers of securities [115], the last time on the basis of data of

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[110] See supra nr. 10.
[111] Naleving van de Belgische Corporate Governance Code: een stand van zaken, by the Belgian Governance Institute and VBO, http://www.corporategovernancecommittee.be/library/documents/EnqueteCodeLippens_0507.pdf
[112] 64% of the companies in the survey published the figure for the CEO (84% for the largest) of which 27% with an "explanation", while 94 % (100% for the largest) published the figure for the aggregate remuneration for the other management members, as called for in the Corporate governance code.
[113] UK Financial Reporting Council, review of the 2003 Combined Code, The findings of the Review, Jan 2006, http://www.frc.org.uk/corporate/reviews.cfm
[114] Assonime, http://www1.assonime.it/assonime/corpgov/ca.nsf/103/FCCA0E45ABAFE5BDC12572900050ED29/$File/FINALE_+26_febbr_analisi+2006.pdf?OpenElement
[115] Assonime and Emittenti Titoli SpA. The last assessment took place in February 2007 and is published as "Analisi dello stato di attuazione del Codice di Autodisciplina delle società quotate" (Anno 2006).

269 companies. Very detailed calculations allow to measure progress in the disclosures. The overall level of compliance is very high, but the document is less explicit on the "explain" option. Some data deserve to be mentioned, such as the analysis of the cases on "independent directors" [116], where the directors evidently were not independent. One will also notice an analysis of disclosures about related party transactions (a large number of companies (91%) have introduced explicit procedures, even providing for fairness opinions), and the finding that 49 (18%) companies declared to be subject to control or direction by other companies, a is now mandated by company law [117]

Germany

Each year, the Berlin Centre of Corporate Governance [118] publishes a report about the state of implementation of the German Corporate Governance code. The 2006 survey was based on a sample of 84 companies[119]. For each of these firms the study checks compliance with the 82 recommendations and 19 "invitations to comply" [120]. The degree of acceptance is almost 100% for the main market, lower for the other market segments (79,3%) [121]. For the firms on the main market, 78,2 out of 82 (or 95,3%) of the recommendations are followed up. Two provisions that remain under the 90% approval rate are the recommendation dealing with the systematic appointment of the top manager to the chair of the supervisory council, and the one dealing with election of members of the supervisory board by individual vote. The publication of the remuneration of directors continues to be opposed by the midsize and smaller firms (55,6%, up from 25%).

Spain

In Spain the securities supervisors follow up on the application of the code as they can also intervene in case of untrue of false or misleading information, and to secure the right interpretation of the definition and concepts of the code. The CNMV report in its bulletin on some of the findings in the application of the code.

49. From this short overview one could deduct that the compliance with the governance codes, as it appears from the surveys that have been consulted, is high to very high, that compliance is stronger for the larger firms, where the role of the markets is more prominent than for the smaller ones, while the more personal details relating to directors and managers (such as remuneration, details about their contract, or about severance payments) continue to be controversial. This has urged some legislators to impose disclosure (e.g. in France[122]). The

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[116] At p. 25 e.s.
[117] Table 22, the latter on the basis of art. 2497 Codice civile.
[118] Berlin Centre of Corporate Governance by Prof. Von Werder, member of the Corporate Governance Commission, Umsetzung der Empfehlungen und Anregungen des Deutschen Corporate Governance Kodex, 20 March 2006; see also U. Noack and D. Zetzsche, Corporate Governance Reform in Germany, the Second Decade, (2005) EBLR, 1033.
[119] Or 28 Dax, 36 Mdax and 20 SDAx firms. The 2007 report has in the meantime be published: see A. von Werder, Presentation at the Press Conference, May 23, 2007, at http://www.corporate-governance-code.de/eng/download/070523_Rede_Von_Werder_en.pdf mentioning that next governance practices are developing.
[120] Anregungen, for which compliance can be waived without disclosure.
[121] Remarks by Dr Gerhard Cromme, at the 6th German Corporate Governance Conference http://www.corporate-governance-code.de/eng/download/Rede_Cromme_en_6.pdf
[122] See the French Companies Act L. 225-102-1 imposing disclosure of directors' remuneration.

surveys also indicate the repeated changes in the Codices, which are often adapted at the demand of the market participants, and the need to update the survey almost every year. The survey in the UK mentioned that the markets in general were quite happy with the status of the disclosures in the UK, and with the overall approach followed. The publication of these repeated assessments maintains the pressure on the firms and keeps their interest in the subject and its possible improvement. These observations make it clear that flexibility in this field is needed and creates a momentum that contributes to improve the degree of response to the codes.

In the absence of any comparable data it is impossible to make a comparison with the degree of compliance with the state imposed regulatory provisions. Due to the presence of explicit sanctions, one can presume this to be relatively high also. However there is a fundamental difference: where the codes organise the way business is dealt with in the sense that business itself would consider acceptable mainly by formulating principles, rather than specific detailed precepts, the law usually imposes obligations that are not so much liked by the firms. Therefore stronger sanctions are needed in the latter case.

Conclusion

Is the widespread use of corporate governance codes a sign that state regulation is receding? Is this the victory of self imposed private law rules over state regulation, and hence, some will say, of private interest over the public good? Some will certainly make a link with political systems, liberalism versus state intervention, and so on. All this is clearly overstated.

It can safely be advanced that corporate governance rules have occupied an important field that previously has been let vacant by state regulation. Business practice, steered by the financial markets has led companies to voluntary introduce practices that the state legislators had not conceived. The pressure of the markets for better and stronger governance is the real driving force behind this movement, not the self-interests of the business world. Therefore it may be found striking but is quite logical that most of our governance rules closely follow ideas that have been developed in systems where the markets are a strong driving force, i.e. the US and the UK. Corporate governance rules and codes, but more importantly corporate governance practice, offer a response to the stronger demands from the markets on company management and governance. Taking into account its flexibility and its business practitioners' origin, called for by the international financial markets, this response could not adequately be given by national legislators, who always remain embedded in their local, national interests. Corporate governance codes are a useful, if not necessary complement to state regulation.

With respect to the relationship with state legislation, the governance codes are at the vanguard of developments. Often the code rules are likely to be included in state regulation after some time and once the experience has reached a state of maturity, the practice can be elevated to the status of a rule (e.g. the requirement to have an audit committee). This process of absorption by the law is not unidirectional: in some case, state regulation will be flanked by corporate practises, such as the voluntary measures to avoid insider trading (Chinese walls, codes of practice, etc[123]) could illustrate. The relationship with state regulation is therefore a changing one, although historically the direction has been towards a stronger solidification of

[123] But these may also be incorporated in the law, especially in the national provisions implementing Mifid.

flexible governance rules into state imposed requirements. In that sense, self regulatory provisions have often been the source of state regulation.

The main test for converting self-regulation into state regulation lies with enforcement: once it appears that the self-regulatory rules are not adequately enforced, the cry for state intervention will increase. Some scandal will trigger legislative initiatives, whereby the tension with the codes becomes explicit. Hence strict implementation of the corporate governance codes is the best guarantee against state intervention. Unfortunately, the common opinion of the business community is not always shared by its individual members, and a gross error by one member may spoil the game for all.

Enforcement of corporate governance codes is essentially a matter for the markets, sanctions being economic or financial, not legal. On this point one sees the difference between self and public regulation. However the question should not be raised in formal terms, but in terms of effectiveness: although there still are some weak spots as has been identified by some of the national monitoring committees, the degree of acceptance and application of the codes is not only better documented, but probably higher than that of many state imposed rules. One may wonder whether it would not be useful to develop legal mechanisms that allow self-regulation to be more effective, without giving it the full teeth of public law.

Financial Law Institute

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