

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

*By Grit Tüngler**

Introduction

The classic large corporations in the United States and Germany appear to share one core common feature: managerialism, which means that power over the enterprise is concentrated in the hands of senior managers, who enjoy large discretion in decision-making. When firm owners bring in these professional managers to act as their agents, the danger is that managers may pursue interests other than maximising shareholder value, so that owners must find ways to control management and to align its activities with their interests. Therefore, from a practical point of view, the task of corporate governance mechanisms is to control managerial discretion to assure that the 'right' decisions are made, or at least that the managers are kept within reasonable bounds.¹

One might wonder why the United States and Germany are the object of the following comparative reflections. While in the 1980s there was a considerable interest in the apparent strengths of the German and Japanese systems of corporate governance, in the mid to late 1990s proponents of the alleged virtues of the US model of corporate governance largely drowned out other voices.² Both in Germany and in the USA, this discussion about the appropriate management and control of enterprises has been under way lately. The purpose of this article is to take a closer look at one of the mechanisms for controlling managers, namely the board structures. The comparison will focus on the ways,

* *Ref jur* Hamburg (Germany); LL.M. (Bond, International Trade Law).

1 D Charny, 'The German Corporate Governance System' (1998) *Columbia Business Law Review* 145 at 148.

2 M O'Sullivan, 'Corporate Governance and Globalization' (2000) 570 *The Annals of the American Academy of Political and Social Science* 153 at 154.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

in which the two systems differ from each other and if there is a model which serves the task of controlling the management board better.

While it is generally assumed by US fund managers and corporate executives that the pressure for control of the management overseas has been an outgrowth of practices developed in the United States, the view from Europe seems to be that revolution in corporate governance sweeping Europe is as American as apple strudel and the Magna Carta.³ Therefore I shall try to answer the question how efficient supervisory boards and independent non-executive directors are in reality and what role the independence of key players within the corporate governance debate plays.

The first part of this article will focus on the German supervisory board and its ability to control the management board of stock companies. In the second part I shall look at the Anglo-American unitary board and the ways in which independent non-executive directors have an effect on corporate governance. Reflections on the connected topics of gradual convergence, harmonisation and unification will conclude the comparative analysis.

The German Two-Tier Board

Whereas American corporations are run under the supervision of a single board, German corporations are organised under the Stock Corporation Act and have a two-tier system. This structure is obligatory for all stock corporations irrespective of their size and workforce. The board is divided into management board (*Vorstand*) and supervisory board (*Aufsichtsrat*). Members of one board cannot sit as members of the other board and managerial functions cannot be delegated to the supervisory board.

Although most German practitioners and legal scholars consider the two-tier board system preferable for corporate governance tasks, it has been admitted, that the functioning of the two-tier board has to be improved. In order to describe areas of criticism more closely, first a short overview of the two-tier board system will be given, followed by a closer look at the supervisory board reform as one of the major subjects in the debate on legislative reform.

The Dual Board Structure

3 See (Anonymous) 'True or false: Corporate governance is an American export' [June 1999] *Global Finance*, 56.

The management board

The management board is in charge of the management of the company according to its own business judgment and represents the company in its business dealings and in litigation.⁴

The supervisory board

Herrmann Abs, former CEO of Deutsche Bank AG and perhaps the most prominent manager of the German postwar era, stated 'It is easier to grab a pig at its soapy tail than to hold the manager of a German corporation liable'.⁵ Therefore, the focus of the supervisory board's work has begun to shift more and more towards advising and counselling the management board. The rationale of monitoring companies' management is no longer perceived to be a question of detecting past mistakes but rather of preventing them from being made in the first place.⁶ From this follows the importance of controlling and supervising the management in time in order to prevent worse consequences. As a kind of continuous representative of the shareholders between their meetings, the supervisory board is supposed to be the guardian of their interests.⁷ These duties and the appointment of a management board are the main tasks of the supervisory board.⁸ Apart from that it calls shareholders meetings, examines the annual financial statements and provides a written report on the result of the audit for the shareholders meeting and represents the company in its dealings with members of the management board.⁹

4 §§ 76 (1), 78 (1) AktG.

5 See B Singhof and O Seiler, 'Shareholder Participation in Corporate Decisionmaking under German Law: A Comparative Analysis' (1998) 24 *Brooklyn Journal of International Law* 493 FN 269.

6 Schneider-Lenné, quoted in JP Charkham, *Keeping Good Company* (1995) 50.

7 § 111(1) AktG; see also H Henze, 'Prüfungs- und Kontrollaufgaben des Aufsichtsrates in der Aktiengesellschaft' (1998) *Neue Juristische Wochenschrift* 3309; B Singhof and O Seiler, 'Shareholder Participation in Corporate Decisionmaking under German Law: A Comparative Analysis' (1998) 24 *Brooklyn Journal of International Law* 493 at 560.

8 Its constitution is regulated specifically in the AktG (§ 96), the Betriebsverfassungsgesetz 1952 (§§ 76 et seq), the Montan- und Mitbestimmungsgesetz and the Mitbestimmungsgesetz 1976, see R Birk, 'Germany' in A R Pinto and G Visentini, *The Legal Basis of Corporative Governance in Publicly Held Corporations* (1998) 53 at 61.

9 K J Hopt, 'The German Two-Tier Board - A German View on Corporate Governance' in K J Hopt and E Wymeersch, (eds), *Comparative Corporate Governance* (1997) 3 at 6.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

Focus On The German Supervisory Board

Since in other legal forms of business organisation like the limited liability company (GmbH) and limited partnership (KG), ownership and control are more closely aligned, the public limited company (AG) with its three mandatory organs management board, supervisory board and general meeting stands at the centre of this analysis.

I will focus on the supervisory board as the main monitoring body in large German stock corporations. The reason for this is that notwithstanding the relative independence of the management board, it is the case in Germany, as in the United States, that the supervisory board normally receives the great bulk of the criticism whenever internal corporate control fails to prevent catastrophic or near-catastrophic behaviour by individual members of the management board or other senior managers, or whenever a company merely performs poorly.

One example for this criticism is the case of the collapse of the real estate empire of Jürgen Schneider. He was convicted in 1997 for talking banks into insufficiently secured loans, leaving his largest creditors with outstanding loans of about \$ 700 million.¹⁰ The investigation of evidence brought the shortcomings of the banks' internal supervision to the surface in particular. After this incident major German banks especially have lost credibility as monitors of managerial performance.

Appointment

Shareholders elect their representatives on the supervisory board, while employee representatives are elected by the workers of the corporation or appointed by the trade unions for a term between four and five years.¹¹

Composition

The size of the supervisory board varies according to the number of workers employed. With the exception of special regulations which apply to the coal, iron and steel industries, the employees elect either a third or the half of the members of the Supervisory Board, depending on the size of the corporation. The one third equal footing co-determination applies, according to the Labor-

10 See J N Gordon, 'Corporate Governance: Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany' (1999) 5 *Columbia Journal of European Law* 219.

11 § 102 (1) AktG; K J Hopt, above n 9, at 5.

Management Relations Act 1952, to all corporations with at least 500 but fewer than 2000 employees, and parity co-determination according to the Co-determination Act 1976, in companies with a workforce exceeding 2000.

Chairman

The supervisory board elects a chairman and a minimum of one vice-chairman, § 107 (1) AktG.

Committees

It may also form subcommittees to prepare negotiations, and to control the implementation of decisions, § 107 (3) AktG.

Facts that May Affect the Supervisory Board's Independence and Ability to Control Management

In general supervisory boards have successfully fulfilled their 'watch dog' function to prevent serious abuses. Therefore, legal theory and practice support the two-tier system in Germany and fundamental reform of the supervisory board is not seriously debated in Germany. Nevertheless, the efficiency of control remains subject to criticism, because the supervisory board's function as the agent controlling the management board is affected, when the supervisory board allegedly became part of the management and has lost its ability to objectively monitor the management board.

This chapter deals with the question, if the sometimes claimed change of the supervisory board into an organisation for business contacts and friendships, where members occasionally work to perpetuate each other's power and perks has taken place and how such shortcomings might be prevented in the future.

Conflicts of interest

Strong position of banks

One of the more frequent criticisms of the German model is that the shareholder representative component of supervisory boards of these companies tends to be dominated by representatives of a few large German banks as well as by a small number of other individuals, many of whom also have close business or professional relationships to the company on whose board they sit.¹² This could

12 TJ Andre, 'Some Reflections on German Corporate Governance: A Glimpse at German Supervisory Boards' (1996) 70 *Tulane Law Review* 1819; Deutsche Bank, for example, recently set up a company to manage its massive holdings of major

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

imply, that at least these supervisory board members might be chosen for the very reason that they are not independent, because they or the particular constituency they represent have an existing financial or similar relationship to the company.

The real influence and economic power of the banks stem from the combination of supervisory board seats, stock participations, bank proxy votes¹³ and the banks credit and underwriting business.¹⁴ Examples for the opportunity of supervisory board seats are the management board members of the three biggest German banks, which are represented on the boards of 21 of the 24 nonfinancial DAX companies.¹⁵ Deutsche Bank alone is represented on the supervisory boards of more than 400 companies.

One reason for companies having bank representatives on their supervisory boards is the significantly positive correlation between credit volume and the number of bank representatives on the borrowers' supervisory boards.¹⁶ Furthermore, the debt ratio is higher if a bank representative chairs the supervisory board.¹⁷ Bank representatives on the other hand use the supervisory board as a platform to establish and to maintain intercompany links. This incentive for bank representatives seems to be one of the potential misuses of the board that might reduce intensity of control, because by representing both themselves as significant shareholders in their own right and their trustees, eg through the voting rights conferred on them, banks exert control, in pursuit not of the interest of all of those individual shareholders who have given their proxies, but mainly in pursuit of their own and possibly conflicting interest.¹⁸

industrial companies. In the process the cozy ties between banker and company, developed in post-war Germany, in which banks provided both debt and equity capital to client companies, has been severed. DB Investor, as the Deutsche Bank company is called, manages funds in excess of DM45 billion (US\$27 billion). Other German banks have also been untangling their financial holdings with client companies, see *Economist*, 12 August 1999.

13 See ER Schneider-Lenné, 'The Role of the German Capital Markets and the Universal Banks, Supervisory Boards, and Interlocking Directorships' in N Dimsdale and M Prevezer, *Capital Markets and Corporate Governance* (1994) 284 at 291.

14 KJ Hopt, above n 9, at 11.

15 Deutsche Bank, Dresdner Bank, Commerzbank.

16 S Prigge, 'A Survey of German Corporate Governance' in KJ Hopt and E Wymeersch (eds), *Comparative Corporate Governance* (1997) 943 at 960.

17 Ibid.

18 Ibid.

Problem of interlocking directorships

Apart from this strong position of banks, one might also view interlocking directorships as a problem of German corporate governance.¹⁹ These directorships are established if a member of one supervisory board is also a member of one or more other supervisory or management boards of another corporation.

This development has given rise to conflict of interest issues. Although the question, if a person with several mandates is able to fulfil his monitoring duty sufficiently, can only be judged on a case-by-case basis, multiple mandates surely are a potential source of inadequate monitoring due to time constraints and personal links which may serve to entrench a group of persons and companies apart from the shareholders' interest.²⁰ For example, it is theoretically possible that management board members share proprietary information or take other action in their capacity as supervisory board members that would benefit one of the companies to the detriment of the other.²¹

One recent example of interlocking directorships is the case concerning the hostile takeover attempt of German steel manufacturer Krupp to swallow its biggest competitor Thyssen in 1997.²² Two directors of the Thyssen supervisory board were also on the board of directors of the banks financing the offer and had been informed of the planned takeover tender. Furthermore, a member of Deutsche Bank's management board sat on Thyssen's supervisory board, and current and retired Dresdner Bank management board members sat on the supervisory boards of both Thyssen and Krupp.²³

According to the predominant view, in that case a director is not bound to resign from the supervisory board of the target company. Resignation is only compulsory when the conflict is permanent. Nevertheless the directors have to refrain from participating and voting in board meetings dealing with the subject of the takeover attempt where the interests of the company are seriously threatened.

19 See for example T Raiser, 'Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?', (1996) 35 *Neue Juristische Wochenschrift* 2257 at 2259.

20 Ibid, at 958.

21 TJ Andre, 'Cultural Hegemony: The Exportation of Anglo-Saxon Corporate Governance Ideologies to Germany' (1998) 73 *Tulane Law Review* 69 at 133.

22 See A Stengel and C Steven, 'Germany' Special Supplement April 1998, 23 at 24.

23 S Prigge, above n 16, at 995.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

It has also been argued that a member of a supervisory board should not be allowed to be a member of either of the boards of a competing company.²⁴ According to representatives of the business and banking sector, the problem lies in determining whether a company is a competing company.²⁵ Moreover, the present law provides that a member of a supervisory board may not be on the boards of more than ten corporations. This still seems to be a large number and not a sufficient provision to prevent the above-mentioned disadvantages of interlocking directorships.

To enhance transparency, which would make personal linkage at least more obvious, the Bill on the Control and Transparency of Companies (KonTraG, 1998) provides that candidates for supervisory boards of quoted companies must disclose their offices and mandates before the election.

Other personal links

There exist further personal links that cast doubt on supervisory board members' willingness to control the management in the stakeholders interest. In these situations members of the supervisory board are so closely connected to management that they become unwilling to act in compliance with the statutory requirements imposed upon them. Collegiality might thus make them hesitant to commence an action against those who run the business, even when uncovering clear evidence of managerial misbehaviour.²⁶ This observation is supplemented by evidence which shows that the additional power of the supervisory board to dismiss members has not been used much. One suggestion to prevent network conflicts of interests is the establishment of judge made rules on conflicts of interest.²⁷ Self-regulation should also play a more important role here.

Co-determination

One reason other than tradition for the requirement of the two-tier structure is Germany's system of labour co-determination. The aim of co-determination is the promotion of trust, co-operation and harmony.²⁸ The social consensus is still

24 KJ Hopt, above n 9, at 16.

25 Schneider-Lenné, see K J Hopt, above n 9, at 16.

26 N Horn, 'Die Haftung des Vorstands der AG nach § 93 AktG und die Pflichten des Aufsichtsrats', (1997) 18 *Zeitschrift für Wirtschaftsrecht* 1129 at 1130.

27 KJ Hopt, 'Common Principles of Corporate Governance in Europe' in BS Markesinis, *The Coming Together of the Common Law and the Civil Law* (2000) 109.

28 J P Charkham, *Keeping Good Company* (1995) 13 and 14 for historical background of employees on the board.

that codetermination is a great achievement because it contributed to social peace between labour and capital.²⁹

Having said that, the question might arise, which role does co-determination play in the actual control of the management board. Although employees are treated as stakeholders in a corporation and employee representatives might sometimes bring an otherwise comatose supervisory board to life - typically in enterprises dominated by the family³⁰ - they are usually not treated as substantial collaborators in the control over management. They have instead been viewed as offering social governance, whereas corporate governance provides firm-level governance.³¹ In fact, co-determination is viewed as influencing the performance of firms neither negatively nor positively,³² so that some criticise a mere illusion of control. A further argument in favour of this view is the fact that in a direct conflict the chair can be counted upon to break a tie in favour of the shareholders. Another unfortunate aspect of co-determination is the frequent tradeoff between management and employees, which can be a disadvantage to shareholders and to efficient control of the management.³³ Apart from that the participation of labour representatives might in some cases cause a ritualisation and fractionalisation of the meeting that precludes an open and potentially controversial exchange of views, thus fostering the problem of undiscussibility and making separate meetings of each bench before a board meeting a common practice. There is also the fear that employee representatives do not strictly observe the principle of board secrecy. As a consequence of the efforts of seeking informal contact the position of the ordinary supervisory board member is weakened and the chairman's position strengthened.³⁴

It has also been conceded by employees union officials that a lack of knowledge in the fields of accounting and finance among employee representatives can be observed. Because of these backdrops some commentators in the most recent reform debate have criticised boardroom co-determination for weakening effective supervision by the supervisory board. Members of the shareholder bench also pass a negative judgment on supervisory board co-determination.

29 K Pistor, 'Codetermination: A Sociopolitical Model with Governance Externalities' in MM Blair and MJ Roe (eds) *Employees and Corporate Governance* (1999) 188.

30 JP Charkham, above n 27, at 23.

31 K Pistor, above n 28, at 163.

32 MR Theisen, 'Empirical Evidence and Economic Comments on Board Structure in Germany' in KJ Hopt *et al* (eds), *Comparative Corporate Governance - The State of the Art and Emerging Research* (1998) 259 at 260.

33 JP Charkham, above n 27, at 46.

34 S Prigge, above n 16, at 966.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

Despite the major criticisms an abolition of co-determination seems out of the question. Therefore an attempt to counteract this development has been made. This is the trend toward electing more professionals to the supervisory board.³⁵ Another attempt to avoid the disadvantages of co-determination is the following one. Although the introduction of quasi-parity codetermination in 1976 extended labour representation in large companies, available data show that many companies changed their by-laws or the rules governing the internal affairs of the supervisory board in expectation of the enactment of the 1976 law or shortly thereafter, usually in a way that restricted the powers and responsibilities of the supervisory board.³⁶

Therefore the situation regarding co-determination is rather disappointing, especially since co-determination has tended to pit the two benches of capital and labour representants against each other, rather than to unite them in the task of controlling management. Thus - and unfortunately so - the predictions of *Mertens* and *Schanze*³⁷ made in 1976, when the respective law was enacted seem to become true, since practice shows that co-determination has set the rules for multiple-party corporate governance in such a way that the net beneficiaries are those who ought to be controlled: the company's management, while the codetermined supervisory council 'as an institutionalized battlefield of interests'³⁸ seems to lose the few control mechanisms with which it was endowed when it was created as an assembly of shareholders' representatives.³⁹

In this context the recent debate regarding co-determination issues raises even more uncertainties and seems to undermine the efforts toward improved corporate governance. According to the present German Minister of Labour Riester, for example, more and also more powerful works councils are needed for co-determination and therefore the laws should be amended.⁴⁰ Such an amendment would probably lead to various backdrops not considered well enough by advocates of this view. According to UPS for example, who considers these suggestions as a gift to the trade unions, one of the negative

35 MR Theisen, 'Empirical Evidence and Economic Comments on Board Structure in Germany' in KJ Hopt *et al* (eds), *Comparative Corporate Governance - The State of the Art and Emerging Research* (1998) 270.

36 K Pistor, above n 28, at 184.

37 HJ Mertens and E Schanze, 'The German Co-determination Act of 1976' (1979) 2 (1) *Journal of Comparative Corporate Law and Securities Regulation* 75-88 at 83.

38 *Ibid.*

39 *Ibid.*

40 See M Schäfers, *Der Streit um die Mitbestimmung nähert sich seinem Höhepunkt*, *Frankfurter Allgemeine Zeitung*, Nr 34, 9 February 2001, 16.

aspects might be that costs for staff and lawyers rise and firms like UPS transfer spheres of activity abroad.⁴¹

Auditing process

Another point of criticism in the corporate governance debate is the auditing process. The auditor's duty is to check whether the provisions of law and charter are met or whether the documents misrepresent the company's situation.

Although the supervisory board should propose a balance sheet auditor, the general meeting elects the auditor, and the management board appoints him.⁴² It has been criticised that, de facto, it is often the management board that selects the auditor. Apart from that, the role of the auditor should be given more attention and the supervisory board should make better use of the information supplied by him, because only in a minority of companies the auditor's report is delivered to the ordinary supervisory board members.⁴³ Therefore, the members of the supervisory board should in the future be able to read the auditor's report before their meeting instead of only at the meeting itself. A solution could be the Bill on the Control and Transparency of Companies (KonTraG, 1998), which provides for a closer relation between supervisory board and auditor. According to the KonTraG the balance sheet auditor is hired by the supervisory board and his participation at the balance sheet meeting of the supervisory board is mandatory.

Nomination process of new members

The most relevant sources of influence on the nomination of supervisory board members are institutional investors, the full board, the CEO and to a certain extent nominating committees. Candidates are identified by shareholder nomination, internal appointment and – not surprisingly - existing contacts of board members.

Although this nomination process of new members seems to be convenient in general, it also gives the widespread impression that there is often too close a connection between the supervisory and the management board, which can negatively affect the intensity of control exerted by the supervisory board.⁴⁴ This connection manifests itself in the strong influence of CEO and chairman of the

41 'Ein Geschenk an die Gewerkschaften', Frankfurter Allgemeine Zeitung, Nr 34, 9 February 2001 at 16

42 S Prigge, above n 16, at 996.

43 S Prigge, above n 16, at 962.

44 S Prigge, above n 16, at 957.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

supervisory board on the selection of new supervisory board members. Further problems can arise from the fact, that 43 % of supervisory boards include a former member of the management board. It is also common practice for the retiring CEO to move to the supervisory board and often becoming its chairman.⁴⁵ It seems questionable how this chairman could become sufficiently independent of his former 'environment'. On the other hand, his experience could be valuable for the supervisory board.

Size of the supervisory board

The number of supervisory board members may reach 20 in large corporations. Shareholder representatives unanimously share the opinion prevailing among academics that this number is too high for efficient work and orderly discussion and therefore should be reduced. Trade unions successfully oppose this proposal and call it 'an attack on co-determination'. Because of the strong position of employees and trade unions and also due to the influence of the Federal Ministry of Labour the corresponding part of a draft statute was abandoned in the course of the legislation process.⁴⁶

Frequency of meetings

Another point of criticism regarding the German supervisory board was the fact that it met only very infrequently. Now the KonTraG requires at least 4 board meetings. However, these meetings of 4 hours on average are still viewed as insufficient for efficient control. Therefore it can only be suggested that companies provide for more meetings in their by-laws.

Communication and flow of information

The supervisory board usually only meets quarterly. Therefore, the management board must properly inform the supervisory board of its policies for the future conduct of business, the profitability and in general the business of the corporation so that the supervisory board is able to understand the business and guarantee effective internal control. Furthermore the chairman of the supervisory board must be notified of any other important event. The supervisory board may at any time ask the managing board for any other information about the corporation if it considers this necessary.⁴⁷

45 Ibid at 958.

46 Ibid at 956; see also KJ Hopt, 'Common Principles of Corporate Governance in Europe?' in BS Markesinis, *The Coming Together of the Common Law and the Civil Law* (2000) 109.

47 KJ Hopt, above n 9, at 6.

From this it follows that it is the management board that sets the agenda, prepares the meeting documents, and sends these documents on behalf of the supervisory board chairman to the board members. This means, that the management is in a good position to control the meeting and the information flow to its monitors.

Moreover, the larger the supervisory board, the stronger the feeling of members that they were not being given enough information and that more frequent meetings than the above mentioned usual 4 times a year are required for effective control. Therefore it has been suggested that monthly reports by the chairman of the management board should be a standard requirement and a general policy report on the stock corporation and its business is indispensable.⁴⁸ However, despite the problems regarding the flow of information from the management board to members of the supervisory board, no standards for the information provisions of the supervisory board by the management have emerged so far.

Formation of special committees within the supervisory board

One solution to the problems of poor communication due to infrequent meetings and the large number of supervisory board members could be the establishment of special committees within the supervisory board. The German legislature has not made the setting-up of committees obligatory, but for many years they have been provided for by the by-laws (charter) of most companies.⁴⁹ German law also provides that the supervisory board may form subcommittees to prepare negotiations and to control the implementation of decisions.⁵⁰

Currently, committees other than the staff and board committees still seem rare. In only about 75 per cent of corporations have committees of the supervisory board have been formed. Examples are personnel committees, chairman's committees, finance committees, investment committees, audit committees, committees for social affairs, co-determination and for ad hoc matters.⁵¹ Since interviewed board members already highly recommend the establishment of committees⁵² it remains to be seen whether this is due to an expected gain in efficacy or only intended to circumvent co-determination requirements. Not only an enhanced committee work in general but also the introduction of an

48 E Scheffler, AG 1995, 207 (210) .

49 Theisen, above n 24, at 261.

50 § 107 (3) AktG.

51 KJ Hopt, above n 9, at 8.

52 S Prigge, above n 16, at 956.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

audit committee within the supervisory board to improve the control of the management should be the focus of attention in future discussions.

Tenure

Another characteristic, which can cause difficulties in controlling the management board, is the fact, that company rules to limit tenures are almost absent in German law. It is feared, that a long tenure, in combination with the board members' interest in being re-elected - not to mention their age - may diminish their ability to monitor critically.⁵³

Contribution to efficiency

The formal structure, particularly the division of interest representation among different groups and its confinement to a separate board, also seems to perpetuate managerial dominance.⁵⁴ Sources of managers' advantages are superior access to information, control over information flow, de facto independence in day-to day decision-making, and an ability to neutralise conflicting groups by playing them off against each other.⁵⁵ The German two-tier structure does not seem to provide adequate control for these factors, especially since the supervisory board relies on the management board for information in the way mentioned above. However, the advantage of the German system is to place a wide range of representatives on the board. While it appears that they are not sufficiently empowered to limit managers' exercise of discretion, ways have to be found to ensure that the supervisory board works more efficiently in the future.

Suggestions for a More Efficient Supervisory Board

Although the supervisory board has taken its role more seriously in recent years, especially since 'ornamental' directors are not fashionable anymore,⁵⁶ there are various areas, which need to be improved, especially where the division of management and supervisory board is not sufficient in reality. In this regard several attempts have been made and one of the most promising is the KonTraG.⁵⁷

53 Ibid.

54 Charny, above n 1, at 149.

55 Ibid at 150.

56 Charkham, above n 27, at 22.

57 See also Das Gesetz zur Kontrolle und Transparenz im Unternehmensbereich
<http://www.steuernetz.de/praxistips/controlling_rechnungswesen/PT003.html>
<<http://www.complex.de/djn/nachrichten/gesetzgebung/g98021.shtml>>;

Additionally, standards of monitoring seem to be necessary. Therefore German business leaders as well as German academics should give priority to setting up generally accepted orderly supervising principles, which should be tested by German companies.⁵⁸ A way of improving corporate governance via the supervisory board could be an enhanced role of self-governance. If the current issues are not resolved, the supervisory board as a controlling organ will be reduced to a merely formal meeting and not be able to fulfil its role in corporate governance.

The Role of the German Code of Corporate Governance

As an attempt to improve Corporate Governance in Germany the German Code of Corporate Governance ('GCCG')⁵⁹ was put forward in June 2000. The GCCG of the Berlin Initiative Group is characterised by a demonstratively business perspective. It does not follow the juridical focus on separated governing bodies, but considers the problems and processes of company management, which arise in and between the organs of management.⁶⁰

The Code highlights the standards of good management and supervision for companies which develop their value creating activities in and from Germany and contains recommendations for the arrangement of the regulatory framework for managing and supervising a company. The Code, which is directed primarily towards large, listed public stock corporations, is not only intended to promote the quality of company management, but at the same time also serves as a source of information for foreign investors seeking a compact introduction into the basic principles of corporate governance in Germany.

The Code attempts to point out solutions to the problems of German Corporate Governance mentioned above. Interestingly, the Code emphasises the important role of the management board. The former Corporate Governance debate, on the other hand, focused on the supervisory board instead. In the eyes of the drafters of the GCCG rules for controlling the management are still important, but this aspect should not dominate the debate.⁶¹ Apart from that,

M Mattheus, 'Das Gesetz zur Kontrolle und Transparenz im Unternehmensbereich (KonTraG): Frühwarnung und Transparenz nun gesetzlich gefordert' <<http://www.krisenkommunikation.de/a-ne-kon.htm>>.

58 See Theisen, above n 34, at 265.

59 <<http://www.gccg.de/initiative.htm>>.

60 W Bernhardt, v A Werder, Der German Code of Corporate Governance (GCCG): Konzeption und Kernaussagen, (2000) 11 *Zeitschrift für Betriebswirtschaft* 1269 at 1279.

61 Ibid at 1273.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

the Code contains suggestions referring to the election of Supervisory Board members, according to which the supervisory board remains master of the appointments procedure and its decision on the appointment must not be merely a matter of form. Furthermore, the Code promotes more flexible and open structures of communication, for example, occasional joint discussions between the Management Board and the Chairman of the Supervisory Board.

Interestingly, the Code promotes the development of a culture of open discussion in managerial and supervisory bodies. Especially the Chairman of the Supervisory Board should promote openness of discussion in the management board as well as in the Supervisory board. At this point the question of how still remaining problems of secrecy as described above might be avoided in future practice. The Code also emphasises the importance of committees formed by the supervisory board in order to increase working efficiency and independent auditors.

At first, these suggestions seem to be rather general, providing no surprising solutions at all. But here one should keep in mind that the company law serves as the starting point and legal frame of the GCCG. The GCCG does not intend to provide suggestions for reform, but rather suggestions, which complement and describe the existing law. The reason for this concentration on existing law is the consideration, that improvement can be brought about within the framework of the GCCG.⁶²

One might also wonder how effective this kind of best practice might be. The formulation of governance principles in a code below the legal level offers the advantage of being able to adapt standards more flexibly to altered conditions and fresh experiences and thereby serve to de-regulate. In order to provide incentives to follow the GCCG a system of certification or control is desirable. In that case the GCCG would have more than just an explanatory function and instead signify a serious attempt to improve German Corporate Governance.

The Anglo-American System: Change of the Unitary Board?

Characteristic Features of the Unitary Board System

In order to fully understand recent developments in American corporate governance and especially the role of independent directors it seems to be helpful to give a short introduction to the American unitary model.

⁶² Ibid at 1271.

Role of the board of directors

The governing structure of a corporation under US law is composed of the shareholders as the owners of the company and the board of directors, who manage or supervise the management of the company.

In a publicly held company the board of directors must serve a dual function of allowing managers the flexibility they need to run the business while setting policy, appointing the principal senior executives, selecting the officers who in reality manage the business and monitoring the managers to limit self-dealing and poor management. The board of directors also reviews the company's financial plans. Therefore the board of directors is sometimes viewed as the cheapest form of consultancy.⁶³ The board acts for the corporation and as a group and traditionally takes actions at meetings usually by a majority vote.

Composition and appointment of the board

The actual role of the board will depend on many factors, including its make-up. There are generally no legal requirements that establish any particular norm for either board make-up or functioning. The number of directors is usually set in the by-laws or certificate and elected by the shareholders at their annual meeting for a one-year term.

Frequency of meetings

Although major US companies tend to be widely dispersed, most boards meet at least six or seven times a year.⁶⁴

Board committees

Statutes generally permit boards to establish committees, which are given particular tasks and can act for the board. Many corporations have executive, finance, nominating, audit and compensation committees.⁶⁵ These serve a useful function allowing for fewer directors to focus on important issues.

63 John M Nash, President of the National Association of Corporate Directors, Washington DC, see B J Reiter, 'Independent Directors' (1999) 63 *Ivey Business Journal* 57.

64 Charkham, above n 27, at 190.

65 AR Pinto, 'The United States' in AR Pinto and G Visentini, *The Legal Basis of Corporate Governance in Publicly Held Corporations* (1998) 253 at 261; see also E Carson, 'The Development of Board Sub-Committees' (2000) 18 *Company and Securities Law Journal* 415 at 416; N Calleja, 'To Delegate or Not to Delegate: Board Committees and Corporate Performance in Australia's Top 100 Companies' (1999)

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

Tendency of Majority of Independent Non-Executive Directors

Many of the recent corporate governance proposals have centred on debates to strengthen the board of directors by appointing more independent directors. While many publicly traded corporations already have some or even a majority of independent directors, they are not required by law.

The independent non-executive director

Compared with to executive directors

Executive directors are members who are also full time officers of the company. They report directly to the CEO and depend on him for their board seats, promotions and salaries. Therefore, they are unlikely to participate openly and critically in effective evaluation and monitoring of the CEO. Non-executive directors, on the other hand, are non-employee directors⁶⁶ and not directly affiliated with the corporation.

Independence

In order to answer the question, if boards can be independent and intimate actors in corporate strategy at the same time,⁶⁷ one has to look at the notion of independence. Independence can to be defined both in relation to the management and to the dominant shareholders. The term requires that the director does not have interests in or relationships with either the corporation or the significant shareholder and fairly reflects the investment in the corporation by shareholders other than the significant shareholder.⁶⁸ Facts, which can have an impact on independence, are the number of directorships held by the outside directors, length of tenure on the board and the length of CEO's tenure in office.⁶⁹ While it would probably be unrealistic to require completely independent directors, it should rather be asked, if the non-executive director is at least willing to put his relations and personal interests, for example within the corporation or outside his own company, aside and in this way is independent enough to fulfil his monitoring task.

66 MP Dooley, *Fundamentals of Corporation Law* (1995) 182.

67 RW Oliver, 'The Board's Role: Driver's Seat or Rubber Stamp?' (2000) 21 *The Journal of Business Strategy* 7.

68 TSE Dey Report 1994, see BJ Reiter, 'Independent Directors' (1999) 63 *Ivey Business Journal* 57.

69 Laura Lin, 'The Effectiveness of Outside Directors as a Corporate Governance Mechanism: Theories and Evidence' (1996) 90 *Northwestern University Law Review* 898 at 903.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

*Traditional role - 'Baubles on a Christmas tree'*⁷⁰

Until recently, it has been argued that neither theory nor practice permits the conclusion that the independent director can be as successful a monitor of social responsibility as it is claimed he is, or even as he may be, as a monitor of integrity.⁷¹ And in the context of social responsibility, even more than in self-dealing, it has been said that there was reason to believe that the losses from using him as a substitute for regulation will exceed the gains. It has also been stated that the argument for the independent director rarely disentangles his possible roles - as a monitor of integrity, efficiency, or social responsibility - or the logic supporting each of them. His leverage in any of these roles has been said to be only modest.⁷²

Changing role

Long gone are the days when Tiny Rowland of Lonrho could famously dismiss independent directors as 'baubles on a Christmas tree'.⁷³ Today, they are a standard ingredient of good company practice - though not required by law - and appear on more and more boards of major US companies. Independent directors are increasingly seen as a countervailing power against the dominant influence on the board, whether of the management - due to the wide distribution of share ownership⁷⁴ - or of the shareholders. Therefore, in situations where the shareholders have limited impact on decision-making, independent directors will be seen as a check on the overwhelming influence of the management.⁷⁵

Whether most committees should consist of independent directors is a recent issue of corporate governance. Most of the legal monitoring devices are aimed at trying to get the board with a majority of outside directors to monitor without too much interference. For example, corporations listed on the New

70 C Blackhurst, in *Management Today* (London) May 2000, 69.

71 See for example S T Goldberg, 'Where are Fund Directors when we Need Them?', *Kiplinger Magazine* April 1997: 'When there is money on the line, they sometimes forget that they are working for the shareholders. It isn't hard to find examples of fund directors who are tolerant of high fees, bad performance or both'.

72 V Brudney, 'The Independent Director - Heavenly City or Potemkin Village?' (1982) 95 *Harvard Law Review* 597 at 658.

73 See Blackhurst, above n 63, at 69.

74 E Wymeersch, 'A Status Report on Corporate Governance Rules and Practices in Some Continental European States' in K J Hopt *et al* (eds), *Comparative Corporate Governance - The State of the Art and Emerging Research* (1998) 1045 at 1098.

75 *Ibid*; see also C Tobe, Mutual Fund Directors: Governance Changes Proposed for Independent Directors in the US, (2000) 8 *Corporate Governance* 25.

York Stock Exchange are required to have at least two independent directors and to have a separate audit committee made up of all independent directors.⁷⁶

Examples

Examples for the changing role of independent non-executive directors are the New York Stock Exchange rules and the suggestions of the American Law Institute.

New York Stock Exchange

Corporations listed on the New York Stock Exchange are required to have at least two independent directors and to have a separate audit committee made up of all independent directors.⁷⁷

The American Law Institute Project

The American Law Institute (ALI)⁷⁸ began analysing, restating and recommending changes to corporate law in the USA in 1978. The resulting report, is a comprehensive restatement of corporate governance principles, from the objectives and conduct of the corporation generally to the role of shareholders in takeovers and tender offers.⁷⁹ In contrast to the Cadbury Committee Report, the ALI Project does not define the responsibilities of individual board members, executive or non-executive. It does, however, expressly acknowledge that the management of a large public corporation should be conducted by the employees and officers of the company, under the supervision of senior executives designated by the board of directors.⁸⁰ It therefore suggests a majority of independent directors in large, public corporations. These directors should be free from any significant relationship with the corporation's senior executives. Where board functions are delegated

76 Pinto, above n 58, at 261.

77 Pinto, above n 58, at 261.

78 For further information see ALI, *Principles of Corporate Governance: Analysis and Recommendations* 113-14 (1994); S M Bainbridge, 'Independent Directors and the ALI Corporate Governance Project' (1993) 61 *George Washington Law Review* 1034; C Hansen, *A Guide to the American Law Institute Corporate Governance Project*, The National Legal Centre for the Public Interest, (1995); see also for ALI A Finlay, 'CLERP: Non-Executive Directors' Duty of Care, Monitoring and the Business Judgment Rule' (1999) 27 *Australian Business Law Review* 98 at 108.

79 H Bird, 'The Rise and Fall of the Independent Director' (1995) 5 *Australian Journal of Corporate Law* 235 at 240.

80 *Ibid* at 242.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

to board committees, the ALI Project recommends that such committees should also be constituted by a majority of such directors.

Reasons for this development

This movement toward the appointment of independent directors for listed corporations in order to deal with the problems of adequate remuneration, conflicts of interests and, more generally, control of management and the CEO, not only in the United Kingdom, but also in the USA⁸¹ can partially be explained by various stock market rules which require some independent directors and also by corporate governance rules which the markets themselves have developed. Additionally, investors may prefer corporations with some independent directors and corporations may use these directors to attract investors.

Efficiency of Independent Directors Acting on the Board

General remarks

Advantages

The benefits of improved corporate governance due to the influence of independent non-executive directors are uncertain. However, they seem to be quite beneficial in general, because the described recent development has unquestionably led to much greater confidence on the part of institutional investors, the government, and the public with respect to management and operation of publicly held corporations. Reasons for this are for example not only the fact that insiders may be unwilling or unable to criticise the firm's CEO, who typically is in a position to influence an inside director's career advancement within the firm, but also the fact that a board with a large number of independent directors is less likely to be tolerant of non-value maximising actions that benefit management at the shareholders' expense.⁸²

Disagreement regarding efficiency

Since shareholders accuse non-executive directors of a shameful failure to exercise effective corporate governance⁸³ the question arises how effective

81 Hopt, above n 9, at 12.

82 Lin, above n 62, at 901.

83 See for example R Barker, Commentary: 'Wanted: Shareholder Rights for Mutual Funds' *Business Week* September 1997 at 27: 'In general, independent directors act more like lapdogs for mutual fund management than watchdogs for shareholders'.

independent directors are in reality. It would be difficult to argue that the American system works much better than the German system. In fact, there is substantial disagreement regarding the capacity of independent directors to monitor effectively. There exist two schools of thought.

The supporters of the managerial hegemony theory argue that management dominates the board regardless of its composition.⁸⁴ According to this theory there seems to be but scant evidence that the presence of outside directors on the American boards effectively controls managerial discretion. Limits on information and motivation are inherent, absent greater professionalisation of the directors and higher-powered incentives or making directors more responsive, not to forget the difficulty to give the directors all of the advantages and influence that insiders would have without having them become 'co-opted' into the insider mentality.⁸⁵

Others support the effective monitor theory, which is drawn from financial economics. They argue that independent directors are motivated to protect shareholders' interests because of their desire to protect their reputational capital as 'experts in decision control'.⁸⁶ For example, unlike in Germany, there have been many cases in the last few years of independent directors acting to make major changes including the replacement of the president or CEO and also the creation of standards of conduct for the board. Heads of several major corporations were replaced by the directors including General Motors, Kodak, American Express and IBM.⁸⁷

According to a third view these theories are too simplistic, since results of empirical studies are varying. Some studies indicate a positive relation between the presence of independent directors and financial performance of the firm, demonstrated for example in the case of Kodak and IBM by positive stock price reaction at the announcements of such appointments.⁸⁸ This positive market reaction suggests that the market perceives appointments of additional independent directors to be in the shareholders interest. Other studies⁸⁹ have

84 Lin, above n 62, at 902.

85 Charny, above n 1, at 151.

86 Lin, above n 62, at 902.

87 Pinto, above n 58, at 280.

88 Lin, above n 62, at 923.

89 See A Klein, 'Firm Performance and Board Committee Structure' (1998) 41 *Journal of Law and Economics* 137; S Bagat and BS Black, 'Do Independent Directors Matter?' Working Paper, Columbia University (1997); 'The Relationship Between Board Composition and Firm Performance' in K Hopt et al (eds), *Comparative Corporate Governance: The State of the Art and Emerging Research* (1998), 281; BE Hermalin and MS Weisbach, 'The Effects of Board Composition and Direct Incentives on Firm

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

found that a high proportion of independent directors does not predict better future accounting performance.⁹⁰ The results of the steady do not support the conventional wisdom that greater board independence improves firm performance.⁹¹ According to the studies, there is no empirical support for current proposals that firms should have 'supermajority-independent boards' with only one or two inside directors. To the contrary, there is some evidence that firms with such boards are less profitable than other firms.⁹²

Therefore - while keeping the advantages of independent non-executive directors in mind - no hard-and-fast conclusions from the mixed body of evidence should be drawn. Instead one should try to provide an explanation for the differing results. One likely explanation for the mixed results lies in the multitude of factors other than board composition that can affect a corporation's profitability. Therefore, it may be difficult to isolate the effect of board composition on firm performance, especially since there may be other specific events like CEO dismissal and payment of greenmail, instead of overall financial performance which are more reliable indicators of whether board composition really does make a difference.⁹³

One further possibility is that different firms need different types of boards. In particular, slowly growing firms may need more independent directors to control the conflict between managers and shareholders over what to do with free cash flow that cannot be profitably reinvested in the firm's core business. If these firms are also less profitable than more rapidly growing firms, then a high degree of board independence would be a result, rather than a cause, of whatever is causing the firm to grow slowly and be less profitable.⁹⁴

Group dynamics and boardroom behaviour rather than any particular board composition could also influence the efficient work of independent directors.⁹⁵ One has also to take into account a range of market forces that might reduce or

Performance' (1991) 20 *Financial Management* 101.

90 J Lawrence and GP Stapledon, 'Is Board Composition Important? A Study of Listed Australian Companies' (1999) <<http://papers.ssrn.com/paper.taf?abstract>>.

91 S Bhagat and B Black, 'Board Independence and Long Term Firm Performance' (2000) <http://papers.ssrn.com/paper.taf?abstract_id=133808>.

92 S Bhagat and B Black, 'The Uncertain Relationship Between Board Composition and Firm Performance' (Working Paper No 175, Stanford Law School, John M Olin Program in Law and Economics, 1999) 32. <http://papers.ssrn.com/papers.taf?abstract_id=11417>.

93 Lin, above n 62, at 926.

94 Ibid.

95 See J Lawrence and GP Stapledon, above n 81.

increase the benefits from any one corporate governance mechanism operating on its own.⁹⁶

From these considerations it follows that in the big picture independent non-executive directors do not *appear* to add value. However, it is very important to keep in mind that this only means the studies fail to produce solid evidence supporting the proposition that independent directors add value.⁹⁷ Therefore, one should be cautious when jumping to conclusions from the above studies and instead keep in mind the difficulties related to proving a positive effect of independent directors on overall firm performance. One way of preventing uncertainties arising from the varying studies might be to carry on letting the companies decide which board composition is most suitable for them and not to provide a mandatory majority of independent directors.

Facts that may affect non-executive directors independence and ability to monitor management effectively

Independent non-executive directors who satisfy all of the independence criteria may nonetheless be relatively ineffective monitors because of the following facts.

Personal links

There may be personal or professional relationships between inside and independent directors that do not create a legal conflict of interest but can create bias. It is an old boys' club, the critics say, a self-reinforcing conspiracy against the shareholders and the long-term interests of the company.⁹⁸

The problem seems to lie in the fact that the independent director earns his money by speaking up in time when a company is floundering. This becomes harder to do when it is an old university friend or colleague sitting across the boardroom table whose failings have to be exposed. Non-executives also sit on remuneration committees and assess the pay of their colleagues as 'the last closed shop'.

One example for interwoven relationships in family-dominated corporate mazes is Carnival Cruises Corp, voted by Chief Executive one of the worst boards in 1999. The ruling family is that of Ted Arison, the founder and former CEO of Carnival cruises. His son Micky is now the CEO, his daughter is on the board. The board, as might be expected, is not very independent. There are 16

96 Ibid.

97 Ibid.

98 C Blackhurst in *Management Today* (London) May 2000, 69.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

directors, of which 9 are family members, inside executives of the parent company or affiliates, or representatives of service suppliers to Carnival.⁹⁹

The non-executive director, who is not a family member or close friend, may also have a significant relationship with the corporation, such as serving as its outside counsel or investment banker, which will have brought him into a close working relationship with senior management outside of the boardroom.¹⁰⁰ This might breed sympathy and make efficient monitoring difficult.

Influence of CEO

Furthermore, independent directors who have no other affiliation with the corporation may be beholden to the CEO, at least for their positions. Critics point out that shareholders have no means to nominate directors, short of waging an impractically expensive proxy contest, and that there is no power base within the corporation that is truly independent of management. In such a vacuum, it is open to the CEO to draw or heavily influence the slate of director candidates who are supposed to oversee his tenure.¹⁰¹ Therefore it has been suggested that the position of the CEO should be separated from that of the chairman of the board who should be an independent director.¹⁰²

Serial directors

Another fact that may affect non-executive directors independence and ability to monitor is the case of an independent director who is an executive director of another listed company, because his attempt to engage in effective monitoring may reflect the (low) level of monitoring that they would wish to see from non-executives on their own board.

Communication and flow of information

Another fact that can have, an impact on the ability to monitor effectively might be non-executive directors lack of knowledge about the company. Therefore the effectiveness of non-executive directors is critically dependent on the quality of the information, which they receive, and in larger companies on an appropriate

99 Robert W Lear and Boris Yavity, 'The 5 best and 5 worst boards of 1999' *Chief Executive* October 1999, 48.

100 MP Dooley, *Fundamentals of Corporation Law* (1995) 183.

101 Ibid.

102 J Charkham, above n 27 at 227; M Bradley *et al*, 'The Purposes and Accountability of the Corporation in Contemporary Society: Corporate Governance at a Crossroads' (1999) 62 *Law and Contemporary Problems* 9 at 68.

committee structure which will involve them to the degree necessary for them to do their job, without treading on the toes of the management.¹⁰³ This requires that the executive directors do not reach a position where they are able to control information and possibly exclude non-executive directors from it. One way of achieving this might be relevant provisions of transparency in a code of practice.

Appointment

If the key role of independent directors is to help and act as a check on management, it is troubling to acknowledge that directors are often chosen by that same management and the above mentioned personal preferences come into play, which might not always present the most efficient and preferable solution for the companies prosperity, especially since directors are required to exercise critical judgment of those executives to whom they owe their position.

Further suggestions to enhance efficiency

Apart from the importance of finding solutions to the mentioned shortcomings of the current corporate governance debate relating to independent directors in the US there are further suggestions to enhance the efficiency of independent directors' monitoring.

California Public Employees' Retirement System (CalPERS)

CalPERS as the largest public pension fund in the USA is the initiator of corporate governance initiatives. Its Code of Practice and Aspiration focuses primarily on the board of directors and its relationship with corporate management.

CalPERS also issues Board of Directors Awards to efficient board of directors that set a positive example. In 1999 it paid tribute to Texas Instruments Inc., because the company's board has embraced the value of independence. Its board is made up of independent directors with open lines of communication with senior management to ensure the board does not rely exclusively on the CEO for information. This is a preferable solution for the above-mentioned problem of communication and flow of information. CalPERS also acknowledged the strong committee structure, reasonable compensation and regular evaluations.¹⁰⁴ All these features contribute to efficient monitoring of

103 G Pease and K McMillan, *The Independent Non-Executive Director* (1993).

104 Editorial Staff, 'Apple turns its governance around' *Investor Relations Business*, (New York) 15 May 2000, 15.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

independent non-executive directors and should therefore serve as an example of good corporate governance.

*General Motors Guidelines*¹⁰⁵

CalPERS also credited General Motors Corp. Director John Smale, who received the independent director award, with bringing corporate governance into the mainstream through the GM's corporate governance guidelines, which have become a blueprint for good governance within the industry.¹⁰⁶

The origin of GM's guidelines was the turmoil on the governance front, which the company experienced, in the early 1990s. Following two years of losses totalling US \$ 11.7 billion in the US division, the independent directors moved in to demote the top three executive directors and restructured the executive committee to include a non-executive director.¹⁰⁷ Smale is one of the key individuals in the evolution of corporate governance who has brought corporations to the point where they value good governance. Nearly every major company in America has followed the lead of GM and instituted corporate governance guidelines.¹⁰⁸ The guidelines brought the obligations of a board of directors to the shareholders and clarified the role the board is theoretically supposed to play with an emphasis on the independent director's role. For example in a situation where a member of management was chairman of the board, Smale publicly advocated having a non-executive director serving a lead role.¹⁰⁹ The guidelines also suggest a majority of independent directors and a board size of 14 -15 members. Another positive aspect is the flexibility regarding term limits and former CEO board membership. The guidelines suggest that these matters should be decided in individual instances. The annual assessment of board's performance by a committee on director affairs is a further important point worth consideration when discussing models for improving the role of the German supervisory board.

Uniform code of practice

105 See text of the guidelines in Hopt and Wymeersch, *Comparative Corporate Governance* (1997), Annex II/8, M-49.

106 Editorial Staff 'Apple turns its governance around' *Investor Relations Business*, (New York) 15 May 2000, 15; see also Editorial Staff, *Harvard Business Review on Corporate Governance* (2000) 191.

107 G Pease and K McMillan, *The Independent Non-Executive Director* (1993) 38.

108 Editorial 'Apple turns its governance around' *Investor Relations Business* (New York) 15 May 2000, 15.

109 Ibid.

While there is the Cadbury Code in England and the Viénot commission in France, there is not a uniform code in the US that defines good practices in corporate governance. This might be due to the fact, that the number of players in the US market are much more diverse than they are anywhere else in the world, including for example charitable organisations, religious organisations, unions, corporations and investment managers.¹¹⁰ Nevertheless there already is a lot of convergence around standard practices. One example is the exemplary role of the General Motors Guidelines. A uniform code of practice should be aimed for in order to ensure that more companies have a transparent and efficient working board of directors. Steps like insisting on independent directors owning more shares, or being more completely independent of management could be worth trying. Companies should be free to experiment with departures from the norm of a supermajority-independent board.¹¹¹

Comparative Analysis

Aim of the Comparison

The simple enumeration of similarities and differences of corporate governance and control of the management in particular are not the aim of this comparative analysis. The purpose of this comparison is to find out in which ways the different models of controlling the management board, despite their differences based on different national attitudes and the political consensus that prevails in the individual states,¹¹² can set positive examples for situations, in which the other system seems to be less efficient.

Comparability

In Germany, where boards are composed as a coalition of representatives of either capital or labour, the issue of independent directors seems to be pointless at a first glance. However, the notion of non-executive directors can not only be found in the one-tier board model of the USA, but also in the two-tier board model of Germany, where outside directors are the basis of the German supervisory board. Especially the problems arising in the context of the control of the management remain similar in both systems. Therefore one comparable

110 See (Anonymous), 'True or false: Corporate Governance is an American Export', *Global Finance*, June 1999, 56.

111 S Bhagat and B Black, 'The Uncertain Relationship Between Board Composition and Firm Performance', (Working Paper No 175, Stanford Law School, John M Olin Program in Law and Economics, 1999) 38. <http://papers.ssrn.com/papers.taf?abstract_id=11417>.

112 See for example U Blaurock, 'Steps Toward a Uniform Corporate Law in the European Union' (1998) 31 *Cornell International Law Journal* 393.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

aspect is the technical structure of approaching the problem of efficient control of the management.

Board Model

Although most of the same issues like, for example, conflict of interests and problems of exchange of information between management and controlling board, are met in both unitary and two-tier board structures, the attempts to solve them are fundamentally influenced by the structure of the board.

Germany

The German corporate governance structure contains a more formalised set of countervailing mechanisms against inside management. While insiders constitute the management board, this board is in turn monitored by the supervisory board. Instead of reacting adequately and flexibly to the changing demands of 'real life', German legal scholars and the highest German court for corporate matters have remained hesitant to change the strong doctrinal framework governing corporate law. Apart from slight changes after the KonTraG in 1998 extensive reformatory efforts can probably not be expected in the near future.

USA

The American model does not have such a rigid and detailed legislation as the German law of corporations. Rather, the source of the flexible protective provisions is a company's own constitution and practice or for example part of securities regulation as administered by the Securities Exchange Commission. In larger companies, the actual functioning of the board of directors may - depending on its composition - not be very different from the way the two-tier board's functions, except that in terms of legal duties and responsibilities the tasks have not been differentiated in the strict way they have been in the theory of the German two-tier model.¹¹³

Upon closer inspection, the seemingly fundamental difference between the structure of the unitary and two-tier model appears less marked, especially since the two-tier model is mandated by German law only for the 5,500 stock corporations. Other companies, like the 650,000 GmbH, are free to have a one-tier or a two-tier board.¹¹⁴ Furthermore there is a clear movement towards

113 K Hopt *et al* (eds), *Comparative Corporate Governance - The State of the Art and Emerging Research* (1998) 1096.

114 KJ Hopt, 'Common Principles of Corporate Governance in Europe?' in

independent non-executive directors who are part of the one-tier board but have special functions. Therefore the structural difference between the board models lies more in theoretical considerations, while in the unitary model in many cases management and control are divided in a way very similar to the two-tier model.¹¹⁵

Special Characteristics Of The Board

Since the structures of both models seem to reconcile, the question remains whether either solution is adequate to meet the problems raised by the present conditions.

Role of the board

Both the role of the supervisory board as well as the role of the unitary board arises out of need for control of the management. Whereas the role of the unitary board is monitoring the management primarily in the shareholder's interest, the supervisory board's task is supervising in the interest of a wider range of stakeholders of the company. In fact, the essence of the two-tiered structure is the explicit representation of stakeholder interests other than of shareholders: no major strategic decisions can be made without the cooperation of employees and their representatives.¹¹⁶

The supervisory board theoretically plays a monitoring role somewhat similar to that played by independent directors on a unitary board.¹¹⁷ But the analogy is clearly a limited one. In a narrow legal sense, the directors of a US board acting in their capacity as directors generally have identical responsibilities whether they are outsiders or insiders. By contrast, the supervisory board concept originated as a kind of substitute for regulation that had previously been undertaken by the state.¹¹⁸

Composition

BS Markesinis, *The Coming Together of the Common Law and the Civil Law* (2000) 105 at 108.

115 Ibid.

116 M Bradley *et al*, 'The Purposes and Accountability of the Corporation in Contemporary Society: Corporate Governance at a Crossroads' (1999) 62 *Law and Contemporary Problems* 9 at 53.

117 CJ Meier-Schatz, 'Corporate Governance and Legal Rules: A Transnational Look at Concepts and Problems of Internal Corporate Management Control' (1988) 13 *The Journal of Corporation Law* 431 at 443 FN 67.

118 Andre, above n 12 at 1825.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

German supervisory boards, quite aside from the labour representatives, may be more diverse than the typical US board. This can be explained by the stakeholder concept.

Supply of information

In both systems the supply of information to the monitoring board in a timely fashion and in a form and of a quality appropriate to enable it to discharge its duties is an important issue. Many believe that codetermination has undermined the potential controlling capacity of the German board.¹¹⁹ For example, the desire to avoid revealing information to employee representatives means that supervisory board members typically receive much less information than American public company directors.¹²⁰ Apart from that, the German supervisory board meets less frequently than the US unitary board. This might imply that the non-executive directors in the US board are better informed and therefore better able to monitor the management. Here the US model should serve as an example.

Committees

Whereas a number of companies in the USA have created very active committee structures to improve corporate governance, most German companies have fewer board committees than their US counterparts, and there are also some legal limits on what functions can be delegated to any committees that have been created. This can be explained by the fact that there is have been efforts to evade codetermination, for example, by establishing supervisory board committees that excluded employee representatives but that were vested with some of the full board's power. Although this particular gambit has been rejected by the German courts, which did not permit those committees which entirely exclude employee representatives,¹²¹ committees will play a more important role in the future of German corporate governance. One of the committees, which have already received more attention in Germany in recent discussions and especially in the KonTraG, is the audit committee as an important force in board life.¹²² The committee building practice therefore seems

119 MJ Roe, 'German Codetermination and German Securities Markets' (1998) *Columbia Business Law Review* 167.

120 JN Gordon, 'Corporate Governance: Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany' (1999) 5 *Columbia Journal of European Law* 219 at 222.

121 *Ibid* at 232.

122 RAG Monks and N Minow, *Watching the Watchers: Corporate Governance for the 21st Century* (1996) 169.

to be one of the areas where the German system approaches the American example.

Board size

One may also observe that the supervisory boards of the largest German companies tend to be considerably larger than the typical unitary boards of comparably sized publicly traded corporations in the US,¹²³ a fact that has not gone unnoticed by German commentators. Because large boards make efficient discussion more difficult it should be tried to reduce the German board size. But however preferable the smaller board size might be, as already mentioned above, the reason for the larger German board size are the co-determination rules, which probably will not be changed in the near future. The reasons for this are political considerations, including the strong role of workers unions. This point is a good example for the embedded features of the German model, which cannot be changed by overtaking the clearly preferable American example.

Independence

In Germany there has been some apparent recognition of the possible benefits of independence between academics and representatives of shareholder organisations, especially when it comes to the problems related to personal linkage of supervisory board members. While there have been some calls for more independent supervisory boards, particularly in light of some recent financial 'scandals' like the one of Jürgen Schneider, it remains the case that most German companies are still a long way from achieving the kind of independent boards to be found in some US companies.

It has also to be kept in mind that problems of board independence are more intractable in Germany than in the USA. This is due to the wider net of personal links of supervisory boards of one company and management boards of another company. The reason for more developed personal linkage is the fact that ramifications of German companies are in general much more common, which also explains why the notion of hostile takeovers is still in its infancy.

German companies should take a closer look at how serious American companies are in trying to enhance corporate governance by means of suggesting a majority of independent directors and codes of practice. Codes of practice like the GCCG, or other guidelines for more efficient working

123 RW Hamilton, 'Corporate Governance in America 1950-2000: Major Changes But Uncertain Benefits' (2000) 25 *Iowa Journal of Corporate Law* 349 at 361.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

supervisory boards could mean a step ahead in German corporate governance. Forms of self-regulation instead of hard and fast rules, which do not fit in every individual case, should be drawn up.

Another aspect that could serve as an example for German boards is the model of Warner Lambert Company, which has been voted one of the best American boards. Its code of practice provides for a self-evaluation process, which consists of soliciting questionnaire responses from every director and having them collated by an outside firm. The report is sent to the governance committee chairman, who is responsible for providing feedback to the board and the CEO.¹²⁴

One suggestion for enhancing the independence and efficiency of the unitary board model is to continue adding truly independent directors, ie representatives of large stockholders who have no other relationship to the company. Moreover, the standard practice whereby retiring senior managers, and in particular the Chairman of the management board, are elected as monitors should in most cases be rejected.¹²⁵

From these remarks it follows that the question is not, which system is better, but rather which substantial differences remain after comparing the corporate governance systems. It seems that the differences remain in the written law of both systems. When it comes to the role of the boards in corporate governance in reality in German two-tier board model seems despite its different theoretical structure work in a similar way, facing almost the identical problems of the unitary board model. Especially the attempts to circumvent co-determination provisions in some of the German boards shows the discontent with the current model and also the need for more efficient solutions than the one sought for in the KonTraG. Because of similar underlying problems the US model should provide at least some food for thought.

Gradual Convergence

One of the most interesting current debates in corporate law is whether the gradual convergence already advocated at least for some parts of civil law in Europe worldwide corporate governance also will ultimately converge on a single model in light of the increasing globalisation of capital markets.

124 RW Lear and B Yavity, 'The 5 best and 5 worst boards of 1999' *Chief Executive* October 1999, 48.

125 Andre, above n 20, at 154.

Sceptics

Convergence sceptics focus on embeddedness of governance systems in national political structures that tend to protect both entrenched insider interests and non-shareholder constituencies against the incursions of Anglo-American governance agendas.¹²⁶ These scholars believe the two systems of corporate governance can co-exist in a globally competitive world.¹²⁷ They argue that reform of legal rules has been slow, impeded both by German resistance and by the difficulties of coordinating rules within the European Union. Thus, they suggest that claims of convergence towards a formally defined set of investor protective governance are clearly premature.¹²⁸

Optimists

Optimists, however, believe that convergence towards a set of similar institutions may not depend on convergence in formal rules. It has been stated by some scholars, that a certain convergence of the two types of boards is occurring, which is only in part imposed by the legislator and stems in part from the needs and the chosen practice of large enterprises.¹²⁹ They offer the following main arguments.

126 JN Gordon, 'Corporate Governance: Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany' (1999) 5 *Columbia Journal of European Law* 219.

127 See, eg, M J Roe, 'German Populism and the Large Public Corporation' (1994) 14 *International Review Law and Economics* 187-202; Shleiffer & R Vishny, 'A Survey of Corporate Governance' (1997) 52 *Journal of Finance* 737 at 769.

128 Charny, above n 1, at 165.

129 KJ Hopt, above n 9, at 12.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

Market forces

Firstly, optimists focus on the evolutionary pressures of competitive international capital markets. They contend that the forces of globalisation and worldwide competition for capital will eventually force corporations to shift to the contractarian paradigm with unitary board to set corporate goals and implement governance systems. Revealing in this respect is the statement of Jürgen Schrempp, CEO of Daimler Benz 'I think we have changed Daimler-Benz - not in a totally Anglo-Saxon sense, because I think there are some great benefits in Germany, but I think we have moved in that direction.'¹³⁰ Keeping also the recent changes at Siemens, Hoechst, and Deutsche Bank in mind, it is suspected that one may look back on the changes within Daimler-Benz as a pivotal moment in the transformation of the German corporate governance system.¹³¹ Furthermore, a 1992 research paper by Oxford Analytica, an English consulting group, identified possible developments in corporate governance in the seven leading industrialised countries (G7) over the next decade. It predicts that the fluid, worldwide capital market will have immense effects on governance. As asset managers seek to invest abroad, they will be attracted by those markets with the most open, shareholder-friendly governance structures.¹³²

Cross-border acquisition as a further convergence route

Another argument in favour of the convergence approach is the role of cross-border acquisition as a further convergence route. For example, in the case of the world's largest cross-border merger of two industrial corporations Daimler-Benz and Chrysler Corporation, the resulting business entity will be a German corporation with a German corporate governance regime. Here German corporate law is surprisingly open to American-style shareholder activism. Therefore, it is likely that the German takeover of a US corporation will lead to a substantial injection of American-style shareholder capitalism¹³³, which will

130 A Taylor III, 'Gentlemen, Start Your Engines' *Fortune* June 8, 1998 at 138, 146, see D E Logue and J K Seward, 'Anatomy of a Governance Transformation: The Case of Daimler-Benz' (1999) 62 *Law and Contemporary Problems* 87 at 106.

131 M Bradley *et al*, 'The Purposes and Accountability of the Corporation in Contemporary Society: Corporate Governance at a Crossroads' (1999) 62 *Law and Contemporary Problems* 9 at 71.

132 R A G Monks and N Minow, *Watching the Watchers: Corporate Governance for the 21st Century* (1996) 310.

133 J N Gordon, 'Corporate Governance: Pathways to Corporate Convergence? Two Steps on the Road to Shareholder Capitalism in Germany' (1999) 5 *Columbia Journal of European Law* 219 at 224.

also have effects on the supervisory board. An important part is played by the 'Integration Committee'. This governance innovation takes place in the form of a shareholders' advisory committee with the task of consulting with the management board 'in connection with the combined businesses and operation' of the company. The committee consists primarily of the shareholder representatives of the supervisory board and the two co-chairs. This means a far-reaching governance change and an effort to bring in American-style board monitoring of managerial performance that avoids the limitations of a supervisory board. From this it follows that it is not impossible that there will be an increased conversion of the German supervisory board model toward a structure quite similar to the unitary board model in the future.

Harmonisation

Closely linked with the convergence debate is the discussion of attempts to harmonise the different models of corporate governance.

European Union

Probably due to the different social-economic background reformatory efforts within the European Union and the attempt of the 5th Directive have not been very successful.¹³⁴ The fact that for example the United Kingdom rejects the two-tier board whereas the majority of German business leaders as well as German academics reject the one-tier board model¹³⁵ leaves not much hope for a fruitful discussion at the present time. Scholars and politicians involved in the debate should keep in mind that the best way of reaching an understanding for the aim of harmonisation of laws in Europe is to show the already existing convergence routes. If the countries are able to choose between the systems as suggested by the Draft 5th Directive instead of forcing a particular system upon a state so that in the end a competition of systems takes place with the more efficient model emerging as the 'winner', harmonisation of corporate governance models in Europe might succeed.

OECD Principles

European harmonisation attempts are accompanied by the development on the global level with the emergence of international corporate governance principles. The OECD Council called upon the OECD to develop, in conjunction with national governments, international organisations and the private sector, a

134 See K J Hopt, 'Europäisches Gesellschaftsrecht - Krise und neue Anläufe' (1998) *ZIP* 96 at 105.

135 Theisen, above n 34, at 260.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

set of corporate governance standards and guidelines. The OECD established the Ad-Hoc Task Force on Corporate Governance to develop a set of non-binding principles that embody the views of Member countries on this issue.¹³⁶

The OECD suggests an umbrella set of governance principles internationally, within which it would be possible for national environments and companies to develop detailed governance structures appropriate to their circumstances.¹³⁷ It does not advocate any particular board structure and maintains that there is no single model of good corporate governance, but some common elements that underlie good corporate governance. According to the OECD the responsibilities of the board should be the following points.¹³⁸ The board should be able to exercise objective judgment on corporate affairs independent, in particular, from management. Boards should also consider assigning a sufficient number of non-executive board members capable of exercising independent judgment to tasks where there is a potential for conflict of interest. Examples are financial reporting, nomination, executive and board remuneration. Furthermore the principles emphasise that board members should devote sufficient time and that they should have sufficient access to information. Also quite useful is the suggested annual audit conducted by an independent auditor.

The OECD Principles take up the main points which have been raised above and it will be interesting to see to what extent the principles will be used as answers in the current American and German debate on corporate governance.

Unification

Since there are indications of convergence of the corporate governance models suggestions have been made to introduce one unified board system. The question is not only, whether this is feasible at all, but also whether this is desirable at the present time.

Although this is difficult to believe and should not be regarded as a serious attempt of unifying corporate governance standards, CalPERS announced in 1996 that it would seek to export some of the corporate governance initiatives

136 Ad Hoc Task Force on Corporate Governance, 'OECD Principles of Corporate Governance' SG/CG (99)5 16 April 1999.

137 See also Sir R Hampel, 'On Corporate Governance' (1999) *Company Director* 12 at 16.

138 See Ad Hoc Task Force on Corporate Governance, 'OECD Principles of Corporate Governance' SG/CG (99)5 16 April 1999; also JH Farrar, 'The New Financial Architecture and Effective Corporate Governance' (1999) 33 *The International Lawyer* 927 at 950.

for which it had become well-known in the USA to four countries in which it had its largest overseas investments: France, Germany, Great Britain and Japan.¹³⁹

CalPERS originally identified six core 'Global Corporate Governance Principles', which are allegedly 'minimum standards to which all markets, throughout the world should strive to adhere.'¹⁴⁰ These principles comprise for example 'accountability' requiring the development of a 'strategic vision' for the company and 'transparency' which requires that companies 'strive for a recognised international accounting standard.' Further suggestions are Codes of Best Practices and to focus on sustained shareholder value.¹⁴¹ It has been recognised that these core principles are on the border of platitudes and do not provide adequate standards by which to measure the governance practices of individual companies. CalPERS recommends in specific principles adopted for Germany, that a 'substantial number' of board members should be independent and that major committees consist 'mainly' of independent directors. Furthermore it suggests a simplification of the proxy voting system and basing the board structure on independence and accountability.

This institutional activism has often been viewed with considerable suspicion or outright mistrust, especially because these suggestions are far too general. Instead they are a good example for how unification should not be tackled. Since unified law has to evolve, it is a mistake to attempt to impose one state's corporate governance system on another state. Therefore CalPERS suggestions should be treated as ethnocentrism not worth serious contemplation when searching for solutions for the German governance problems.

Conclusion

After making these comparisons the focus of attention should be on aspects in need of reform. Beside the criticism already mentioned German law should not cling to doctrinal frameworks and instead take firm-specific characteristics more into account. Internal business conflicts should be resolved flexibly on a case-by-case basis by the corporation and not in every case by mandatory rules in a court. A good start in this respect is the KonTraG, which tries to avoid further mandatory regulations as far as possible. A related code of practice could be a useful means in this respect. Furthermore, the role of the auditor as a safeguard should receive more attention. Of particular importance are also the

139 Andre, above n 20, at 71.

140 California Pub Employees' Retirement Sys, CalPERS Global Corporate Governance Principles (1997) <<http://www.calpers.ca.gov/invest/corpgov/cgglobe.htm>>; see also Y Wu, 'Honey, CalPERS Shrunk the Board!' (Chicago 2000) ssrn.

141 Andre, above n 20, at 78.

THE ANGLO-AMERICAN BOARD OF DIRECTORS AND THE GERMAN
SUPERVISORY BOARD - MARIONETTES IN A PUPPET THEATRE OF CORPORATE
GOVERNANCE OR EFFICIENT CONTROLLING DEVICES?

critical reassessment of the close relations between companies and financial enterprises, where considerable pressures for change have built up.

The debate in the US should possibly broaden the range of interests to consider in corporate governance. Further current proposals include mandatory term limits for directors, specific retirement ages for directors and CEOs, limits on the size of boards and limits on the number of directorships in different corporations that a single individual can hold. The further development towards a majority of independent directors is also useful to improve monitoring the management.

Although it has been said the advantage of the German system is the clear division of function, the reality suggests that the US monitoring mechanism with a distinction between executive and independent non-executive directors achieves better results. In the end there seem to be more areas, where the solutions of the US should serve as an example for the German system. However, this statement should not be judged as advocating a blind adoption of the complete US model, but rather as supporting the search for reform models.

If the criticism is taken seriously in both systems, boards of directors and independent non-executive directors in particular as well as members of German supervisory boards will not be marionettes in corporate governance, but able to fulfil their task of monitoring management efficiently.

If one looks at the recent development not only on a European level but also on a global level, it is impressive, that Rabel seems to have foreseen the importance of taking other legal systems into account when he said in 1958 'Any substantial development will have to be accompanied by a radical turn from provincial to world-wide thinking'.¹⁴² The future will show in which ways global thinking in the corporate governance debate is able to improve national models of corporate control.

142 E Rabel, *Conflict of Laws - A Comparative Study*, (2nd ed, 1958) 105.