

Corporate governance across continents

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An spate of corporate scandals marked the start of this millennium, spawning new corporate governance codes in many countries.

The infamous downfall of Enron, once the world's leading energy-trading company, was part of an avalanche of the biggest-ever corporate scandals. In the aftermath, and that of the spectacular bankruptcies and investor losses that followed, the United States introduced tough new laws. The Public Company Accounting Reform and Investor Protection Act of 2002, commonly called SOX or Sarbox, covers issues such as corporate governance, auditor independence and financial disclosure.

Since then, there has been a virtual explosion of interest in such issues, and many countries and organizations now also have corporate governance codes in place. While their motivations might be similar - to prevent the recurrence of such scandals and to better protect minority stakeholders - the international corporate governance landscape is diverse.

So diverse, in fact, that some U.S. companies now list on foreign exchanges precisely to avoid SOX's tentacles and thereby enjoy more lenient climates.

In order to provide specialist advice to global companies on compliance and its cost in different countries, entire new aspects of corporate consulting have sprung up to deal with the myriad international differences. Does a guidelines-based "comply or explain" approach apply, or are there stricter rules? How should the board of directors be structured? Who can be a member and how should they be remunerated?

In the occasional paper "[Review of Selected Generally Accepted Corporate Governance](#)

[Codes](#)," Przemyslaw Koblut, Josep Tàpies and [Rafael Fraguas](#) of IESE focus on Germany, Italy, Spain, the United Kingdom and the United States. They set out a table comparing the different approaches taken by the four E.U. countries on key common issues. These include:

- *Board of Directors*: its mission and functions
- *Requirements Regarding Directors*: chairman and CEO, number of directors, types of directors, definition of independence, requirements for board members, evaluation of the board, remuneration, reelection and conflicts of interest
- *Committees*: remuneration committee, audit committee, nomination committee, executive committee, among others

According to the paper:

- Germany applies a best-practice approach under the German Corporate Governance Code, introduced in 2002, which deals separately with the management boards and supervisory boards of Germany's two-tier system.
- Italy Corporate Governance Code was issued by the Italian Stock Exchange in 1999 and reviewed in 2002 and 2006. Like Germany, Italy takes a best-practice approach.
- Spain's Unified Code on Good Corporate Governance, introduced in 2005, applies a flexible "comply or explain" approach.
- The United Kingdom pioneered the "comply or explain" approach. The key source of corporate governance recommendations for listed companies is the Combined Code, introduced in 2003 and revised in 2006. Companies must say in their annual financial reports how and where they have complied with the code and where not.
- The United States, via SOX, focuses on companies' internal control issues and regulatory reporting processes. It strictly regulates relations between a company and its auditors.

Overall, the authors find that what the corporate governance codes of other countries treat as best practice in the areas of internal control - such as protection for whistleblowers and auditor independence - SOX treats as law. SOX, on the other hand, does not regulate issues such as board composition, committees (other than audit committee) and so on, leaving those to best practice-type codes.

How much is too much?

The wave of corporate scandals not only refocused attention on executive remuneration, it ignited shareholder fury over fat-cat pay packages and bonuses. So how do the different

countries address this issue for board members?

The paper shows that the United Kingdom urges a little restraint: "Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose."

"A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance," the U.K. code stipulates.

In Germany, the following criteria should apply: "Personal performance, the performance of the management board, as well as the economic situation (and) the performance and outlook of the enterprise, taking into account (that of) its peer companies."

Italy says remuneration "must be established at an amount sufficient to attract, maintain and motivate directors endowed with the professional skills necessary for managing the issuer successfully."

And Spain requires a company's remuneration policy to at least specify "the amount of the fixed components, performance-related components (and) main characteristics of pension systems."

Value and virtue

Ever wondered what keeps board members awake at night or what their main mission is? According to the Italian Corporate Governance Code, it is to "create value for the shareholders." Similarly, Spain's Unified Code on Good Corporate Governance says it's to "maximize the company's value."

The UK's Combined Code takes a slightly different tack, saying the board's mission is to "provide entrepreneurial leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed."

And Germany requires companies' management boards to ensure that "all provisions of law and the enterprise's internal policies are abided by."

There are already calls for a global corporate governance model - to seek more uniform application of best practice and to reduce intercontinental compliance confusion and complexity. But for now, at least, in many countries, there are no excuses for ignorance or

unethical conduct.

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