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A Common Corporate Governance Code

-Mission Impossible?

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1. Introduction

This chapter contains an introduction of the corporate governance and the corporate governance codes, which then lead to the treatment of the problems companies can face in the international financial markets when complying with national codes. The problem discussion then leads up to the aim of our research.

1.1 Introduction to corporate governance and the corporate governance codes

Corporate governance is the essence of our research and we start with a question; what is corporate governance?
According to Parkinson and Kelly (1999) governance is understood to be the relationship between shareholders (who are viewed as the owners of the company) and managers.
Corporate governance can be viewed as 'a system by which corporations are directed and controlled' (OECD 1999; cited by Shah et al 2003).
Melvin (2004; cited by Lufkin 2004) states that corporate governance has come to mean many things, from a description of companies' internal management to the process by which they are directed and controlled.
Turnbull (2000; cited by Shah et al 2003) defines corporate governance as ´the influence affecting the process for appointing those who decide how operational control is exercised to produce goods and services and all external influences affecting operations or the controllers'.
As one can conclude the definition of what corporate governance is, is quite diverse, but internal control and direction of companies are common used words.

The years 2001 and 2002 are partly remembered by the scandals, the dot.com bubble, company failures and the stock market crash. The company- names probably remembered are Enron, World.Com and Xerox; the great scandals of United States.

The scandals were a consequence of weak corporate governance where for example the companies used high- risk strategies without any consideration about the value for the shareholders, where insiders of companies used their own internal knowledge to gain themselves and where executives and directors of companies were rewarded large salaries, stock options and other remunerations in short run perspectives.

The result of the scandals was that the public trust, investors', employees' and pensioners' confidence declined and had to be rebuilt. Necessary reforms for such a work has been; the changing of the board structure, executive pay, auditing, risk management and company reporting as an example (Taylor 2003).

Even if the scandals in Europe were less damaging than in the United States, the European investors' trust have fallen and the investments have been reduced (Trevisan 2004; cited by Lufkin 2004).

During the last decade the discussion about corporate governance has come up to surface and codes of best practice and corporate governance have been adopted as guidelines for companies in countries all over the world.
The codes are aimed at adopting mechanisms for enhancing effective investor protection against the power given to managers of public companies (Alves and Mendes 2004) and will serve to ‘compensate for the lack of the legal systems covering shareholders’ and to re-establish public trust in the system rights (Aguilera and Cazurra 2000; cited by Alves and Mendes 2004).

The implementing of the codes started with the Cadbury report 1992 in United Kingdom, which was the first corporate governance code implemented in the world. The report was a reaction on the recent British scandals in the early 1990’s with companies like Maxwell and Polly Peck. (Trevisan 2004; cited by Lufkin 2004).
There are at least 40 codes of corporate governance at national and international level within the European Union. The high number of codes is explained by differences in legislative and institutional systems of member states. Due to the distrust of investors in the European market, companies have had more difficulties to finance their growth and maintain stock value. This at the same time as Europe is facing a slowdown in the economic growth. Therefore, the European commission recognised the need for a solid system for corporate governance in Europe that would be necessary for a modern, dynamic and interconnected industrialized society; for millions of investors; essential for strengthening the internal market and building an integrated European capital market. (Trevisan 2004; cited by Lufkin 2004).

The year 2002 the European commission set up the high level group of company law experts on modern regulatory framework for company law in Europe. In the report the group came to the conclusion that such a common code would fail since rules would be totally or partly based on national company law, which are in certain aspects widely different from each other. But the group also states that the European union actively should seek to co-ordinate the efforts of member states to improve corporate governance by changes in their company laws, securities laws or in their codes of corporate governance. This is a work to see to that the codes do not necessarily diverge between the member states. (Report of the high level group pf company law experts 2002).

1.2 Problem

Imagine a multinational company that has its core business in Germany but also has other businesses in Spain, Sweden and United Kingdom where it is listed on the countries’ stock-exchanges. This is a situation that multinational companies today face. How can this company build trust in every one of these financial markets to attract capital? The codes are a way of creating trust for the companies in the national financial market but how will such codes create trust internationally when they are so different? The corporate governance codes of each country stated in the example above can be that different that this company will have a hard time to create trust in the British, the German, the Spanish and the Swedish financial market at the same time. Because of the difficulty to create international (European) trust for the company a common code for all European countries could be a solution.

The European commission has come to the conclusion that it is not possible to implement a common code for the member states because of the differences in the national laws. But the before mentioned situation still withstands and is a problem for the international companies when trying to attract financial capital in the international financial markets. We want to examine within what areas and recommendations of the corporate governance codes the difficulties lies to create a European common code and if these difficulties can be explained by the institutional systems existing in the European member states.

1.3 Aim

Our aim is through a comparison of different corporate governance codes and institutional systems analyse what similarities and differences the codes and the systems have with each other and through our conclusions make a final judgement if it is possible to unite the codes into a common code in the European Union.

1.4 Why we believe this research is interesting

We believe our research, treating the question if it is possible to unite the codes of corporate governance existing in the European member states, is interesting because of the willingness to create a single financial European market. We have stated above that countries in Europe to day have different corporate governance codes. This can be a problem when creating a single financial European market. A resolution could be to create a common code for corporate governance in Europe.

2. Method

This chapter describes the method we have used in our research and it shows that we have chosen to do three different analyses, and that we have had to use different approaches in different analyses. Further this chapter contains the discussion how we could use other approaches to come to our final conclusions and gives an explanation why we have chosen to write our research in English. The chapter finally explains the demarcations we have made and the way we have collected data to do our research.

2.1 A summary of our method

Within the European Union many countries have developed their own codes for corporate governance. The aim of our research is to see if it would be possible to unite these codes into one common code for the European Union. To reach our aim we have made three different analyses. In the first analysis (formal analysis) we have analysed four different corporate governance codes in four different countries. In the second analyses we have analysed the institutional systems (for example; ownership-structures, control- structures and voting rights for the shareholders) existing in these countries. In the third analysis (total analysis) we have analysed if the main differences we found between the corporate governance codes could be explained by the institutional systems in each country.

2.2 The formal analysis

In the formal analysis we have chosen to compare corporate governance codes from four different countries. The codes we have chosen are; the British code (the Combined code), the German code (the Cromme code), the Spanish code (Ley Aldama) and the Swedish code (Svensk kod för bolagsstyrning).

The reason for choosing these countries is that they represent different institutional systems existing in Europe. The United Kingdom represents the Anglo-Saxon system, Germany represents the Germanic system and Spain represents the Latin system. We have also chosen to look into the Swedish corporate governance code since Sweden represents an institutional system existing in between the other three country systems (with a well developed financial market like in United Kingdom, with concentrated ownership and the importance of banks like in Germany and with important family ownership like in Spain). The Swedish code is also interesting to analyse since it has been approved during our research and therefore is an up-to-date analysis.

We have used an inductive approach to do our formal analysis because we have made a research without basing it on former theories and because there is no single model for a corporate governance code. Therefore we have had to divide the codes into different parts, trying to find a structure that could fit them all. This new-made structure has then made it possible for us to compare all the codes. The structure we found to be the most appropriate is the one showed by our analysis- model (page15). In each part of this model we then made a detailed comparison to find the similarities and differences between the codes. Then we put the information into tables to make it easier for us to see these similarities and differences. To further ease the comparison we named one part of table only, which shows when there is only one code stating such recommendation. In our conclusions we have then tried to conclude if the recommendations in each code is easy or difficult to unite into a common code based on the main differences.

We do not believe that we could do our research of the codes in another way because we have not found any model to compare the codes. Therefore we have followed our own analysis-model.

To do this inductive research all necessary information has been available, which are the corporate governance codes. Therefore if our analysis is missing some part this depends on that we have missed important information rather that we have not had enough of information.

2.3 The Institutional analysis

In this part of our research we have looked into the institutional systems existing in each of the four countries (United Kingdom, Germany, Spain and Sweden). To do our research of the institutional systems we have used a deductive approach since we have read literature already stating which institutional systems that exist in Europe and which parts that signifies such systems. Although we have chosen to use the institutional model dividing the systems into Anglo- Saxon, Germanic and Latin systems we have looked into special features for each institutional system existing in each of the four countries stated above. Therefore we have sometimes concluded that the Anglo-Saxon system represents United Kingdom, the Germanic system represents Germany and that the Latin system represents Spain. Sweden is not represented by such system and therefore we have searched information to find the features of the Swedish system. Of all the information we have found about each system we have tried to pick out the parts of the systems that can explain why the corporate governance codes differ since the aim of the research of the institutional systems is to find an explanation about the differences in the codes.

2.4 The total analysis

In the part called; the total analysis our goal is to find if the differences in the codes (formal analysis) can be explained by the differences in the institutional systems (institutional analysis).

If there are explanations of the differences between the codes in the institutional system we will conclude that such recommendations will be hard to unite in one common code within the near future. This depends on that institutional systems are hard to change because they depend on history, norms, cultures, laws, etc. If differences between the codes cannot be explained by the institutional systems we will conclude that such recommendations could be put into one common code.

To do this analysis we have used an inductive approach since we have used qualitative data from the formal analysis and the institutional analysis and made our own conclusions of how the institutional systems can explain the differences in the codes. To do this we have not used a certain model, but we have tried to explain such differences through discussing how each difference in the code can be explained by the different features in the institutional systems.

2.5 Other approaches

It would be hard for us to use a deductive approach when comparing the codes since we have not found an existing model to do so. Therefore we had to create our own analysis model to compare them.

It would also be hard for us to use another approach than the deductive when analysing the institutional systems. If we would use an inductive model we would have to go to the different countries and look into the presence of certain features explaining the behaviour in each country.

We do not believe that we could use another approach to do the total analysis either, since we have not found any model explaining the connections between the codes and the institutional systems.

Although we could not use different approaches we could have started with analysing the institutional systems and through that analysis directly find the special features of these systems. This could then had made our research of the codes easier in finding the special recommendations of the codes that is making it hard to unite the codes into one common code.

2.6 English

We have chosen to write our research in English to avoid as many translation-mistakes as possible. When writing in English we have avoided translating three of the codes (British, German and Spanish) into Swedish, while we instead have had to translate the Swedish code into English. Mark that the German and Spanish codes are already translated once before and when we compared some of the recommendations, which seemed strange in the translated codes, we found that certain translations from the original codes had been wrongly made. Therefore we have chosen to translate the Swedish code into English instead. Maybe we can also use the wrong words in English but at least in the Swedish code we understand everything and the translation will not be depending on that we have misunderstood something in the code.

2.7 Demarcations

In the analysis of the institutional systems we have made the choice not to look into national law existing in each country, therefore it is a demarcation of the research of the institutional systems.

Much more literature could have been read about institutional systems before doing our institutional analysis. But throughout our research we have seen that most of the literature brings up the same basic features and explained them approximately in the same way. Therefore we believe that the literature we have studied is enough to make a conclusion about the typical features in each system.

The sample of countries for our research is also a demarcation, when we have chosen just to look into four countries, although we believe that the chosen codes are a good sample of the European member states since they represent three different systems existing in Europe.

2.8 Data collection

To do the formal analysis we have had all the information available, which are the recommendations stated in the corporate governance codes.

Our institutional analysis is based on data collected from; articles in databases, articles found on Internet, articles in newspapers and books. Most of the data we have collected is articles we have found in the database Elin at Kristianstad Högsskola and at the University of Lund. To find these data we searched for words like "corporate governance", "corporate governance codes", "corporate systems", "institutional systems", "ownership structures" and "comparative corporate governance".

3. Introduction to the corporate governance codes

In this chapter we are briefly going to introduce the four different corporate governance codes, on which we have based our formal analysis.

3.1 The Combined code, United Kingdom

United Kingdom has a history of codes. The Cadbury code, which was the first code in United Kingdom and also in the world, was implemented 1992. This code has been a pioneer in the field of corporate governance and has become a model for the self- regulation of boards in other countries. Since 1992 there has been a large extent of reports on corporate governance in United Kingdom; 1995 the Greenbury report treating executive remuneration, 1998 the Hampel report treating committees on corporate governance, which was the first code called the combined code, 1999 the Turnbull report stating guidelines for directors, followed by the Myners reports 2001 treating institutional investors in the United Kingdom. The now existing Combined code was implemented 2003 and is a combination of the Smith report made the same year treating audit committees and the Higgs report also made the same year treating the role and effectiveness of non- executive directors. (Bernard Taylor, 2004).

The basic view of the work with the British code has been that the governance is understood like the relationship between the shareholders (the owners of the companies) and the managers. The first code (the Cadbury code) was a reaction to scandals and collapses of companies such as Polly Peck and Maxwell. Therefore the British code is built by the purpose to improve the quality of this relationship. (Parkinson & Kelly 1999).

The target group of the code are listed companies. Smaller listed companies, in particular those new to listing, may judge that some provisions are less important in that there case. Investment companies have normally a different board structure, which also may affect the relevance to comply with some recommendations in the code. [1]

The Combined code consists of two main parts named companies and institutional shareholders.
The part called companies is further divided into directors, remuneration, accountability and relations with shareholders. In the appendix of the code there is one part relating to the previous reports on corporate governance; Turnbull, Smith and Higgs.

3.2 The Cromme code, Germany

The German code was implemented the year 2002.

The code contains recommendations for the management and supervision (governance) of German listed companies. The code aims to make the German corporate governance system transparent and understandable. Its purpose is to promote the trust of national and international investors, costumers, employees and the general public in the management and supervision of listed German stock corporations.

[1] The information stated with no literature reference concerning the codes are found in the codes.

Primarily the code addresses listed corporations, but it is recommended that non- listed companies also respect the code.

The structure of the code is as follows. Section one states recommendations about shareholders and shareholders' meeting, section two gives recommendations about the corporation between the Management board (MB) and the Supervisory board (SB), section three gives recommendations about the MB, section four gives recommendations about the SB, section five entails recommendations about transparency and final section, six, gives recommendations about reporting and audit of the annual financial statements.

3.3 Ley Aldama, Spain

The turbulence in the markets during the past years, the scandals and the increasingly intervention of households in the Spanish capital markets have increased the need for a Spanish corporate governance code. Spain is otherwise known for the long tradition of state dirigisme and coordination of the economy with a capital market centred around banks and financial institutions (very often with cross- holdings, concentrated capital ownership and stable hard cores of shareholders) and managers accustomed to having close relationships with the legislative power and little oversight by the board of directors and much less by the shareholders' meeting. But the structure of ownership has changed during the past 10 years since the households' financial assets have increased significantly. As an example it should be mentioned that at the end of 2001 close to 60% of financial assets held by the households were directly or indirectly related to the securities market (equities, bonds, mutual funds, pension funds and insurance), compared with 37% in 1995 and 23% in 1985. By the end of 2002, 28% of the capitalization of the Madrid Stock Exchange was owned by households.

The first corporate governance code called the Olivencia report was implemented in Spain 1998. The now existing code called Ley Aldama was implemented 2003.

The Spanish code addresses companies that issue securities and instruments admitted to listing on organized markets in their relations with consultants, financial analysts and other companies, persons or entities which assist them or provide professional services to them, and those which should apply among the latter, in order to increase the transparency and security of the financial markets in the light of the structural changes, the current globalised market and the trends in the international markets.

The code focuses on listed companies, which are the centre of the capital markets and of the process of raising funds from the public, but its recommendations may also be applied by any company resorting to the primary securities market (issue market) for the first time with the aim to place its securities with the public, whether or not those securities are subsequently listed in a secondary market.

The Spanish code is a surge for protection of the shareholders' ownership rights and the cornerstones of the code are the principle of freedom for the companies to decide on their own and the transparency for outsiders to see how the company is managed.

The report is structured as follows. The first section is devoted to analysing the significance of duty of loyalty, duty of diligence, conflicts of interest and transparency. The following section gives recommendations about the company organs. Next section gives recommendations about professional service providers and the final section gives a number of reflections on the scope of application of the recommendations.

3.4 The Swedish corporate governance code

The Swedish code proceeds from the Swedish corporate law (Aktiebolagslagen, 1975:1385) and the existing self- regulating rules of corporate governance on the Swedish market such as the listing rules and listing- agreements set up by Stockholm Stock Exchange, Nordic Growth Market and AktieTorget, rules set by Näringslivets Börskommitté, statements made by Aktiemarknadsnämnden and the rules set by FAR (förenade auktoriserade revisorer).
The Swedish code was made as a result of the Swedish corporate scandals arisen during the past years and because of the fact that a majority of the Swedish people are today shareholders, direct or indirect, and are affected by how the Swedish companies are managed. Although the Swedish company law treats many of the questions of corporate governance the need to improve and raise the standards or corporate governance was judged to be important.

The purpose of the code is to make a contribution to improve the management of Swedish companies and to promote the trust for the Swedish capital market nationally and internationally. The goals of the code are to create good conditions for the owners to exercise an active and responsible role, create a balance of the power between owners, board and management, create a clear role- and responsibility guideline between the management and the controlling organs, protect the minority shareholders and create best possible transparency towards the owners, the capital market and the community.

Matters concerning the work of the auditor, the functioning of the financial market place and companies' relations to costumers, employees or other stakeholders are not treated in the code since such areas are not treated as part of corporate governance questions.

The target group of the code are companies with a wide range of owners. Therefore the code is primarily aimed at the market companies, listed on the stock- exchange or other authorized market place. Smaller companies (although listed on a stock exchange) can deviate from the rules since they sometimes can be too hard to implement for smaller companies. A company is considered to be smaller when the board is not bigger than six to seven members (Interview 2004).

The work with the Swedish code began during the autumn of 2003 and the first layouts for the code were ready in April 2004. The final code was approved in December 2004 and is to be implemented during 2005.

The code contains three main parts; the introduction to the code, role of the owners and their responsibility and the rules for corporate governance. The rules for corporate governance is divided into; shareholders' meeting, appointment of board and auditors, board, senior management and the information about corporate governance.

4. The formal analysis model

This chapter contains the explanation of the formal analysis model and how it is used.

4.1 Explanation of the formal analysis model

To be able to analyse the similarities and differences of the codes we had to make our own analysis-model since the codes contained different sections with different recommendations. We have divided our analysis model into; comply or explain, duty of loyalty/duty of diligence/conflict of interest, board, committees, remuneration, shareholders' meeting and reports. The part called board is further divided into recommendations about; composition, independence, size, amount of meetings, age, term limits and CEO/chairman. The part called committee is also divided into recommendations about; nomination-, remuneration-, audit- and other committees.
We have chosen to divide our model into these pieces because we judge them as the most important recommendations in each code.

The pieces of our analysis model are stated and explained below.

4.1.1 Comply or explain

Corporate governance codes are not implemented into national law and therefore there is no penalty if the companies do not follow them. Therefore all codes are built on a comply-or-explain principle, which mean that; if the recommendations in the codes are not followed the companies should explain why.

4.1.2 Duty of loyalty, duty of diligence and the conflict of interest

This part is named differently in the different codes so we have put them together under this headline.
To make this part easier to understand we will explain the different parts:
The duty of loyalty states how directors should manage his/her position in the company, for example not use the company's wealth for own gain.
The duty of diligence states how directors should perform their work, for example in the best interest of the company.
The conflict of interest states how directors should act, if having another interest than the company.

4.1.3 Board

In the part called board we will look at the recommendations for the board in each code and compare them. To make this work easier we have chosen to divide this section into smaller parts that we call the underpinning points of the codes. These underpinning points are composition, independence, size of the board, amount of meetings, age, term limits for the board members and the division of the chief executive officer (CEO) and the chairman.

4.1.3.1 Composition of board

In the part called composition we compare the recommendations in each code of how each board should be composed.
To make this part easier to understand we will explain the difference between a two- tier and a one- tier board structure.
In a two- tier board structure the board consists of a management board (MB) and a supervisory board (SB), which provides the separation between management and supervision of management. The SB has the duty to monitor the competence of the MB and it gives advice on major policy decisions. The MB is appointed and dismissed by the SB. (Weimar and Pape 1999).

In a one- tier board structure there is just one board where executive and supervisory responsibilities are condensed in one legal entity (Jeroen and Pape 1999).

4.1.3.2 Independence

In the part called independence we compare the recommendations of independence for directors in each code.
Independence for directors means that directors in some way are independent to the company, to managers or to owners. Some countries contain such independence criteria since they judge it important for some directors of the board to have a different view of the company that insider directors have.

4.1.3.3 Size of the board

In the part called size of the board we compare the recommendations in each code of the number of directors that should form the board.

4.1.3.4 Amount of meetings

In the part called amount of meetings we compare the recommendations in each code for the amount of meetings that the board should hold each year.

4.1.3.5 Age

In the part called age we compare the recommendation for the maximum age for directors stated in each code.

4.1.3.6 Term limits for the board members

In the part called term limits for the board members we compare the recommendations in each code for how long directors should form part of the board.

4.1.3.7 Chief executive officer/ chairman

This part of the codes states if the Chief executive officer (CEO) can be the same person as the Chairman of the board.

4.1.4 Committees

The part called committees states which committees each code recommends.
Committees are seen as a tool for the board and a way to delegate the work of the board to different specialists called committees. We have parted the committees into five different areas, which we call the underpinning point of the committees. These five areas are called the recommendation of the committees, the nomination committee, the remuneration committee, the audit committee and other committees.

4.1.4.1 Recommendations of committees

In this first part we compare which committees each code has recommended.

4.1.4.2 Nomination committee

In this part we compare the proposed composition and the work of a nomination committee made by each code.
The responsibilities of a nomination committee lies within the area of election, re- election, removal and other proposals of for example directors and managers.

4.1.4.3 Remuneration committee

In this part we compare the recommendation about the composition and the work of a remuneration committee made by each code.
The responsibilities of a remuneration committee lie within the area of remuneration (for example to directors, managers and committee members).

4.1.4.4 Audit committee

In this part we compare the recommendations of composition and the work of an audit committee made by each code.
The responsibilities of an audit committee lies with in the area of audit, for example, election, re- election of auditors and the evaluation of the auditors', the audit company's work and the evaluation of non- audit services.

4.1.4.5 Other committees

In the part called other committees we compare the recommendations of other committees made by the codes.

4.1.5 Remuneration

In the part called remuneration we compare the recommendations of remuneration to directors and managers in each code.

4.1.6 Shareholders' meeting

In the part called shareholders' meeting we compare the recommendation for the meeting in each code about for example the information to shareholders before the meeting, the participation of directors and managers at the meeting and the exercising of shareholders' rights etc.

4.1.7 Reports

In this part we compare the recommendation of which reports should be made and how they should be made available.

4.2 How the formal analysis model is used

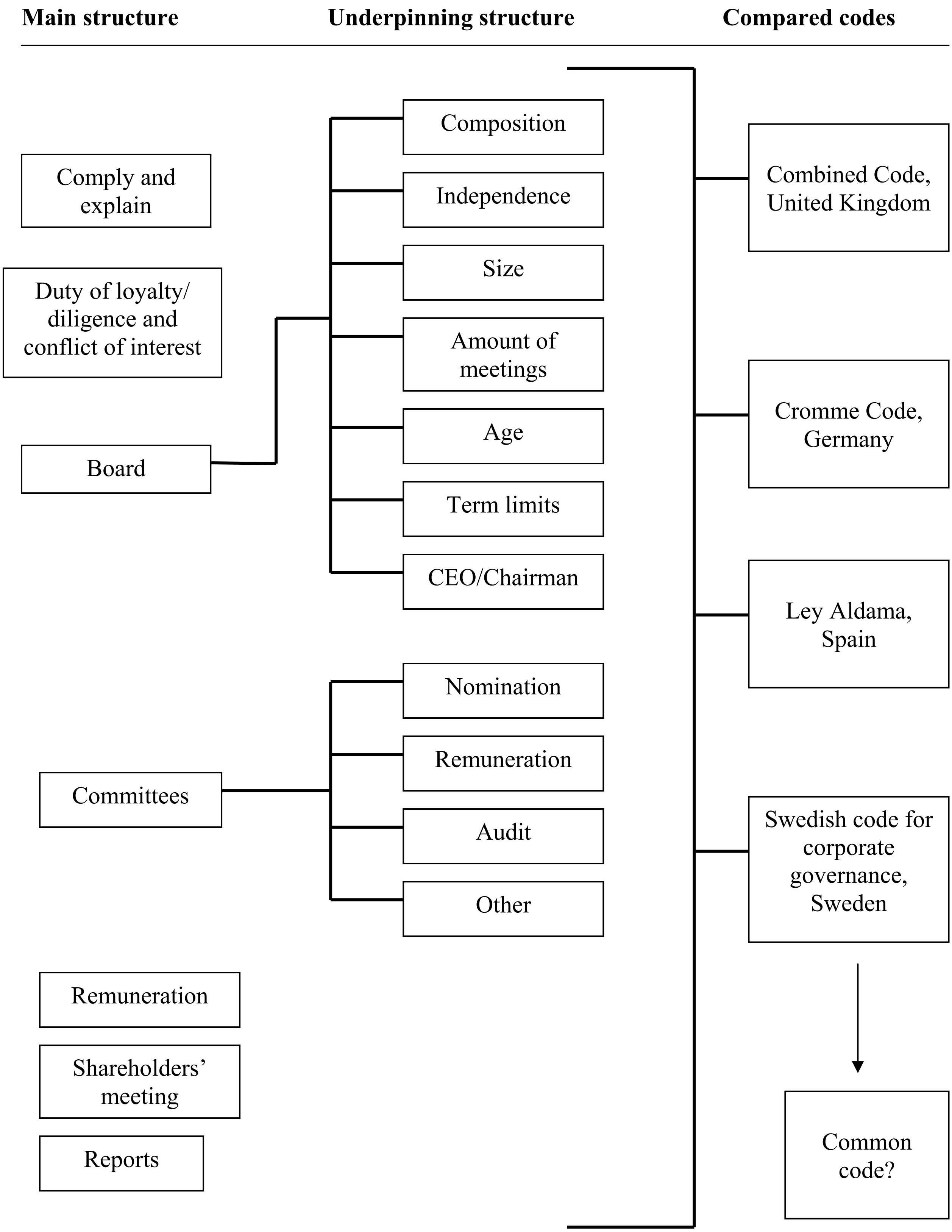
The aim of our formal analysis is through our analysis model find out which recommendations in the codes are similar and which recommendations are different.

To reach our aim of the formal analysis we have used this model to compare the most important recommendations between the codes. To do so we have in each part of the code made a detailed comparison of the codes. To make these comparisons easier to understand we have put them in tables. In the tables we have one column called only, which signals if one code has stated a rule that is not to be found in the other codes. Such recommendations are of significance since they point at a recommendation that can be hard to unite in one common code. Further, in our conclusions, we have then only stated the most important recommendations found in the comparison, which can make it hard or easy to unite the recommendations into one common code.

We have also in each conclusion stated if we believe the recommendations are possible or not to unite.

The analysis model, shown on the next page, shows the parts we have concluded as important in the codes. The model also shows that the aim for our formal analysis is to find out if it is possible to unite the four codes (British, German, Spanish and Swedish) in one common code *(picture 4:1).*

4.3 The formal analysis model in picture



Picture 4:1

5. The formal analysis

In this chapter we compare the British, German, Spanish and Swedish codes through our formal analysis model. Our goal of this analysis and this chapter is to conclude which areas or recommendations that will be easy or difficult to unite. To come to this conclusion we firstly make a comparison of each area of recommendations and then through the help of tables conclude if the recommendations are easy or hard to unite in one common code. Finally we make a summary of all conclusions, which will show which recommendations of the codes that we conclude, through our formal analysis, will be hard to unite.

5.1 Comply or explain

Through comparing the recommendations of how to use the comply or explain principle in each code we will come to the conclusion if such recommendations can be united in one common code or not.

5.1.1.1 Comparison

The British code entails the comply or explain principle where stating that a company has to confirm its compliance with the code's provisions and provide an explanation if non-compliance.

The German code does not contain a special part called comply or explain but states that the recommendations stated with the word shall is obligatory and a non- compliance with such recommendation demands an explanation. The code also contains recommendations using other words but a non- compliance with such recommendations does not demand an explanation.

The comply or explain principle is in the Spanish code expressed as such; when a company departs from the standards for good corporate governance stated in the code it must make a detailed explanation that can be easily assessed by the market. The code also states that the company must regularly review its governance practices and offer a judgement about its degree of compliance, and, where possible, provide data and evidence to support it.

The comply or explain principle is in the Swedish code stated as such; a company can deviate from the rules stated in the code but then have to give an explanation for the reason of the deviation.

All codes state that non- compliance are not stated in regulatory-law and will not be followed by a penalty. It is for the market to decide if explanations followed by non- compliance are acceptable or not. Although not regulatory, each country has implemented a body of regulation to monitor the compliances with the codes.

5.1.1.2 Conclusion

The comply or explain principle is stated almost the same way in every code – a company has to explain how it complies with the code and has to give an explanation if not. There are no penalties; the financial market is to decide if the explanation is acceptable or not.

Since all codes state the comply or explain principle this recommendation is not hard to unite in one common code.

5.2 Duty of loyalty, duty diligence and the conflict of interest

Through comparing the recommendations in the codes concerning duty of loyalty, duty of diligence and conflict of interest we will come to the conclusion if the recommendations can be united in one common code or not.

5.2.1.1 Comparison

The British code is missing a separate part for duty of loyalty, duty of diligence and conflict of interest but states that the directors should devote the necessary time for the assignment on the board.

The German code has a special part about transactions between directors and company (duty of loyalty) where the code states that transactions between MB (management board) or close person and company must follow standard customary in sector. The same recommendation in the code for the SB (supervisory board) is that a member with contracts with the company shall have it approved by the SB.
The members of the MB shall not take sideline activities without the approval of the SB and that members of the MB may not take or give bribes.

The German code contains one part called conflict of interest, which is divided between management board (MB) and supervisory board (SB).
The code states that a member of the MB with conflict of interest shall inform other members of the MB and disclose such conflict to SB without delay.
If a member of the SB has a conflict of interest with the company this shall be informed to the SB, which then shall inform the shareholders' meeting. If such conflict occurs between a member of SB and the company and the conflict is not temporary the director shall terminate his/her mandate.

The Spanish code contains two parts; duty of loyalty and duty of diligence and these two parts are in the Spanish code very specified since it contains a list of different situations of duty of loyalty that a director can be exposed to. For example the code states that directors with conflict of interest should refrain from debates and from voting and conflicts of interest between member or close relative and the company should be notified to the board. The code also states that a member should inform changes that can effect their appointment and also changes in ownership of shares, options and derivatives directly or indirectly. Members should also inform about actions made with impact on the company's reputation and keep insider information secret. There is also a recommendation for not to exploit such information for own gain. These rules are also referred to persons who from the outside can be seen as directors. Note that the controlling shareholders are one of these.

The German and Spanish codes state that a member of a board should/ shall not put own interest in front of the company's interest and state that a member of the board may/should not use company's opportunities or decisions for own gain.
In the Spanish code this recommendation is more specified; assets and positions should not be used to gain patrimonial advantages without consideration, (this is not wrongly translated but

has in English at least two meanings. You can understand this like something you can do if you have thought it through or as if you have done the sufficient work to gain this advantage).

The Swedish code does not have a special part for duty of loyalty, diligence or conflict of interest but recommends the chief executive officer (CEO) and the directors to have sufficient knowledge to do the best work for the company and the owners and give the time and devotion necessary for the assignment. Therefore it is stated that a director shall not have that many assignments that it will disturb the time and devotion needed for the assignment and that he/she shall learn sufficiently about the company, organisation and market that is necessary for the assignment.

The German, Spanish and Swedish codes contain recommendations about that the directors are to work for the best interest of the company. The Swedish code also states that the work should be done in the best interest of the owners. Although no separate part the British code states that directors should work in the best interest of the shareholders (owners).

	United Kingdom	Germany	Spain	Sweden	Only
Duty of Loyalty			Spa		Spa
Duty of diligence			Spa		Spa
Conflict of interest		Ger			Ger
Notify the board		Ger	Spa		
Notify Shareholders' meeting		Ger			Ger
Terminate mandate		Ger			Ger
Not vote			Spa		Spa
Not put own interest ahead company's/best interest of company		Ger	Spa	Swe	
Work in the best interest of shareholders (owners)	UK			Swe	
Not use opportunities or decision for own gain		Ger	Spa		
Time devotion			Spa	Swe	
Transactions between directors and company		Ger	Spa		
Sideline activity outside the company		Ger	Spa		
Not take "bribes"		Ger			Ger
Inform about changes effecting appointment, ownership and company reputation			Spa		Spa
Insider information keep secret not use for directors own purpose			Spa		Spa

Table5:1 ***Duty of loyalty, duty of diligence and conflict of interest***

5.2.1.2 Conclusions

The German and Spanish codes emphasize the importance of guiding directors' work in different situations while the British and Swedish codes judge it more important to emphasize the importance of directors devoting sufficient time for the assignment.
The handling of conflict of interest is emphasized in the German and Spanish codes.
The British code states that the work of directors should be done in the best interest of the shareholders (owners). The work in the best interest for the company is stated in the German; Spanish and Swedish code but the Swedish code also stresses the importance for directors to work in the interest of the owners.

Since there are differences in the recommendations in this part as shown it can be difficult to unite into a common code. The hardest recommendation to unite is in which interest directors should work since it is stated differently in the codes.

5.3 Board

In our analysis model we have divided the recommendations concerning the board into; the composition of the board, independence of the board, the size of the board, the amount of meetings, the age of directors, the term-limits for directors and the CEO/chairman. We will in this section compare each and one of the recommendations between the codes.

5.3.1 Composition of the board

We will in this part compare the different recommendations in the codes stating the composition of the board to come to the conclusion if there is a possibility to unite the recommendations in one common code.

5.3.1.1 Comparison

The German code recommends a two- tier board, which is divided into the management board (MB) and the supervisory board (SB) *(picture 5:1)*.
The MB is responsible of managing the enterprise and SB's task is to give advice and supervise the MB.

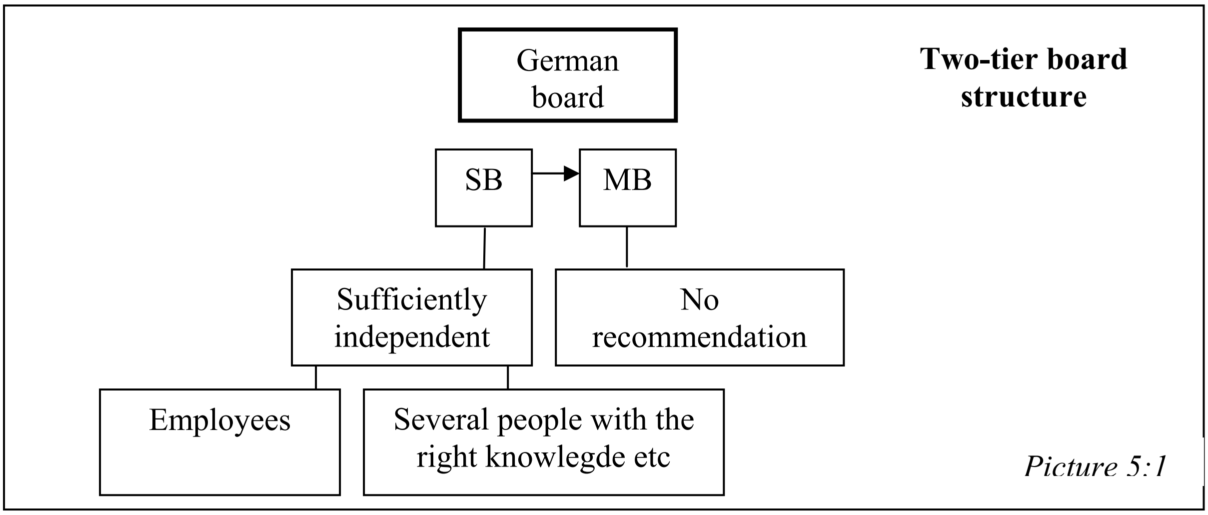
The recommendation for German boards is that they should contain a chairman and several persons with right knowledge, abilities and expert- experience to complete their tasks on the board. The German code also recommends employee representatives on the SB and these rules are specified. If a company has 200 employees one third of the board is recommended to be employees and if the company has 1 000 employees the proportion is recommended to be one half.

The British, Spanish and Swedish codes all recommend a one tier- board system *(picture 5:2)*.

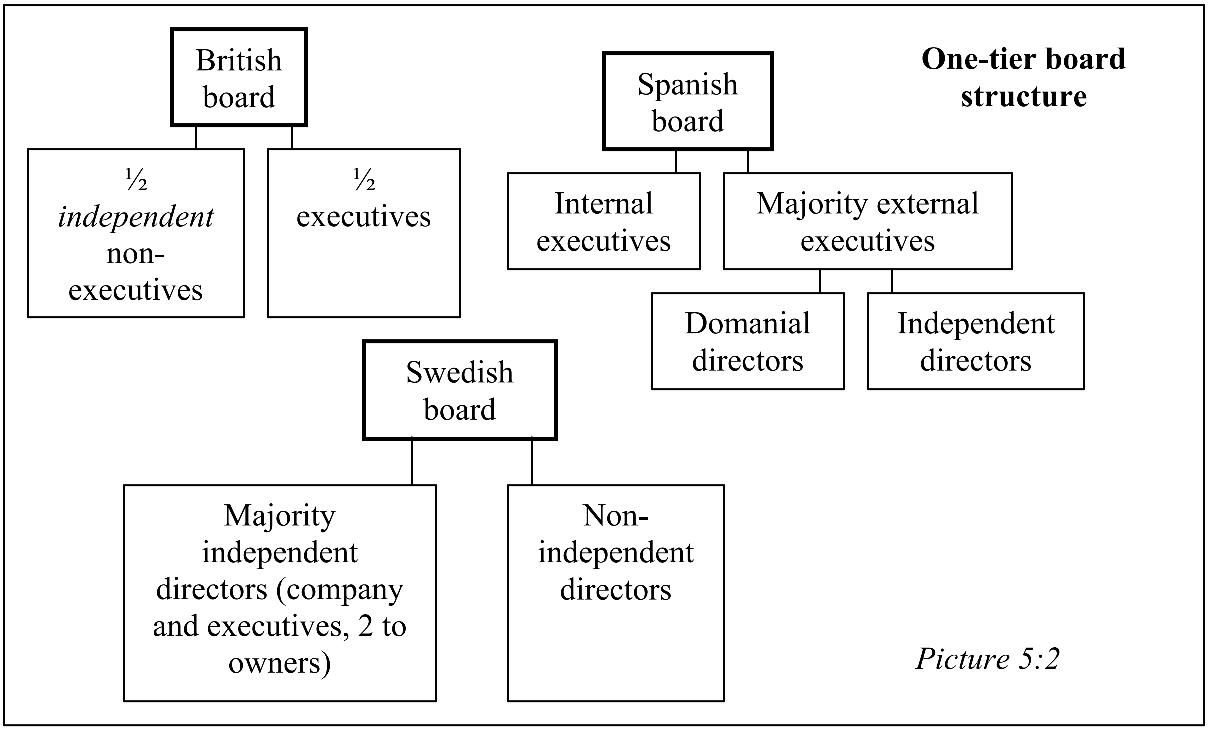
According to the British code half of the members of the board should be independent non-executives and the other part executives. The independent non- executives directors are independent to the company and senior management.

The Spanish code recommends three different kinds of directors of the board; internal/ executive directors, domanial external directors and independent external directors. The external directors are divided into domanials and independent directors. The domanials represent stable shareholders (individually or collectively). The recommendation of the composition is that half of the board members should be external directors.

The Swedish code states that the majority of the board members shall be independent to the executives and the company and that at least two of these shall be independent to large shareholders. Large shareholders are explained as owners with more than 10% of the shares and voting rights in the company. Only one member from senior management can form part of the board. The code also states that the composition of the board depends on the company and the directors' competence and background. The Swedish code also recommends the board to be composed by half men, half women.
The Swedish code refers to Swedish law in the introduction of the code where it states that in companies with at least 25 employees, the employees have the right to elect two representatives on the board and two deputy members. In companies who work in several sectors and with at least 1 000 employees, the employees have the right to elect three representatives and three suppliants but the number of the employee representatives may never be a majority of the board.



Picture 5:1



Picture 5:2

	United Kingdom	Germany	Spain	Sweden	Only
Two- tier board (MB & SB)		Ger			Ger
One- tier board	UK		Spa	Swe	
Independence:	UK	(Ger)[2]	Spa	Swe	
½ board independent	UK			Swe	
½ board external directors			Spa		Spa
Domanial directors			Spa		Spa
Just one director can be senior manager				Swe	Swe
Employee representatives		Ger		(Swe)[3]	
Independence to company and senior management	UK		Spa	Swe	
Independence to all shareholders	UK		Spa		
Independence two at least 2 major shareholders				Swe	Swe
Gender				Swe	Swe

Table 5:2 ***Composition of the board***

5.3.1.2 Conclusion

The most notable difference is that the German code recommends a two- tier board structure while the codes recommend a one- tier board structure.

The German code recommends employee representation on the board but does not recommend independent directors to form part of the board, the other codes are missing this recommendation.

The importance for independent directors to form part of the board is stressed in the British, Spanish and Swedish codes but in the British code it seems more important to close the boards for owners while open them for management while this is seen from the opposite view in Sweden. The importance for owners to form part of the board is also stated in the Spanish code since it recommends externals (owners and independent directors).

An important question in Sweden also seems to be the gender composition of the board and points at the importance for women to form a significant part.

This area is very diverse for all the countries and can be difficult to unite in one common code because of the differences between; the board systems (two- tier and one tier boards), the representation of the employees on the board and the importance of independence.

[2] Signifies sufficiently independence without specific rules stated in the code.
[3] Not according to code but according to Swedish corporate law.

5.3.2 Independence criteria

We will in this part compare the different recommendations in the codes about how directors can be independent and make a conclusion if it is possible to unite such recommendations in a common code.

5.3.2.1 Comparison

The independence criteria in the codes contain almost the same main points; employment, commercial relations, remuneration (although not stated in the Spanish), relationships, years that the director has formed part of the board and interlocking directorship. These criteria shows when a director is not independent.

The British code states that a member of the board is not independent if he/she has been employed by the company within the last five years.

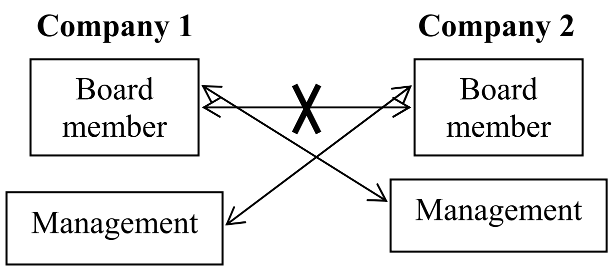
To be independent, a director cannot have or within the last three years have had any material business relations with the company directly, as a shareholder, partner or director. Such director cannot have been a senior employee of a company with such relations with the company either.

Remuneration is another criteria for independence where the British code states that a member of the board is not independent if he/she has received or receives remuneration other than the director's fee, participates in the companies share option or a performance- related pay scheme or is a member of the company's pension scheme. Independent directors should not be given incentive pay.

Relations to other people are one component affecting independence and the British code states a member not to be independent if he/she has close family ties with advisors, directors or senior employees.

The British code also states that to be independent the director should not represent a significant shareholder and that a director is not independent if he/she has formed part of the board more than nine years.

The last criteria in the British code states how independence can be affected by interlocking directorship and the code states that a director is dependent if he/she holds directorship in another board or has significant links with other directors through involvement in other companies' bodies (*Picture 5:3*).



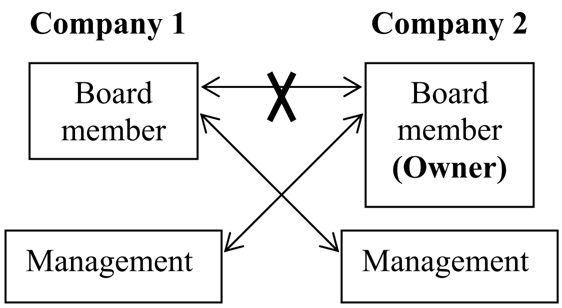
Picture 5:3

According to the Spanish code to be independent a director cannot have or have had an employment within the recent past in the company, group of companies, credit institutions with a significant position in the company's finances or in an organization that receives significant subsidies from the company. We conclude that the recent past lies within three to five years.

To be independent a director can not have or have had a commercial or contractual relation now or in the recent past (three to five years stated above), direct or indirect of significance with the company, its directors, group of companies and credit institutions with a significant position in the company's finances or in a organization that receives significant subsidies from the company.

To be independent a director cannot be a close relative to an executive and domanial directors and to senior managers.

The criterion for interlocking directorship is in the Spanish code stated as to be independent a director can not be a director of another listed company if that company is a owner of the first and has domanial members on the board (*Picture 5:4*).



Picture 5:4

The Swedish code states that to be independent a director cannot be or been employed by the company, a close company, a former owner of the company, an auditor or former auditor of the company during the last three years. Close companies are defined as companies in which the company owns 10 % of the stocks.

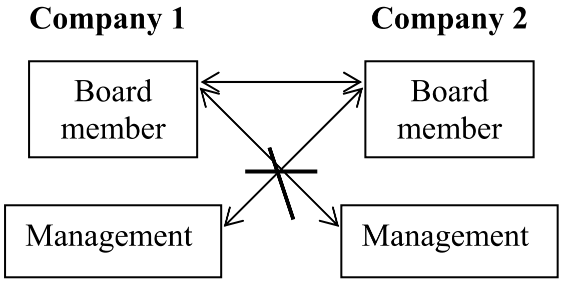
To be independent the director cannot have or within the last year have had significant business relations or other economical relations with the company or close company as costumer, supplier or other co-operative partner. The director cannot be or been a significant owner in another company that have such relations with the company.

According to the Swedish code a director is not independent if he/she receives a significant compensation for advises and services to the company or to close companies (explained above) outside the directorship or if such director receives significant compensation from a manager.

The relationship criterion is stated in the Swedish code to contain close family relations to a person of senior management or other person with direct or indirect contact with the company.

To be independent a director cannot form part of a board for more than twelve years according to the Swedish code.

The Swedish code also states that an independent director can not be or during the past five years been a chief executive officer in the company or close companies and at the same time states that he/she is not independent if he/she is a senior manager in another company, which has a director that is senior manager in the first company (*Picture 5:5*).



Picture 5:5

	United Kingdom	Germany	Spain	Sweden	Only
Employment	UK		Spa	Swe	
The last 5 years	UK				UK
The last 3 years (in company or close company where firm owns 10%)				Swe	Swe
The recent past			Spa		Spa
Commercial relations	UK		Spa	Swe	
Remuneration	UK			Swe	
Not take part in incentive programs	UK				UK
Relationship	UK		Spa	Swe	
Close family ties (advisors, directors & senior employees)	UK				UK
Close relative (executives, domanials, senior managers)			Spa		Spa
Family ties to senior managers (specified) and other persons				Swe	Swe
Interlocking directorship	UK		Spa	Swe	
Time limit of how long the director can sit on the board	UK (9 years)			Swe (12 years)	

Table 5:3 ***Independence criteria***

5.3.2.2 Conclusion

The most significant difference is that the German code does not judge the independence as an important content of the board.

The other codes almost contain the same recommendations although there are some major differences. The British code for example emphasizes the importance for independent directors not to receive incentive pay.
The interlocking directorship is also a notable difference since the Swedish code emphasizes the importance of that the management not influence the independent directors while the British code points out the importance of that independent directors not to form part of two boards. The Spanish code emphasises the importance of that the other board is not a board of an owner of the company.

Because of the differences in the recommendations stated above this area of independence can be hard to put together in a common code.

5.3.3 Size of the board

In this part of our model we will compare the recommendations about the size of the board stated in each code and conclude if such recommendations can be united in one common code or not.

5.3.3.1 Comparison

The codes do not recommend the number of directors but the British and Spanish codes do recommend that the board should not be too unwieldy. The Swedish code states that a board shall not be so large that it becomes ineffective and that the number of members shall depend on the company, on the members and their knowledge and background. The German code is missing any recommendation about the size of the board.

	United Kingdom	**Germany**	**Spain**	**Sweden**	**Only**
Not too unwieldy	UK		Spa		
No recommendation		Ger			Ger
Depends on company and members				Swe	Swe

Table 5:4 ***Size of the board***

5.3.3.2 Conclusion

The conclusion is that according to the Swedish code it is important to look at the composition of the members and how they can improve the work of the board while in the British and Spanish codes it is important for the companies not to have to many members (probably depending on that the work then will be inefficient). In Germany it seems more important that the company decides the size of the board on its own.

This part can be easy to unite in one common code because the different codes have not stated a certain number of directors to form part.

5.3.4 Amount of meetings

In this part of our model we will compare the recommendations about the amount of meetings stated in each code and conclude if such recommendations can be united in one common code or not.

5.3.4.1 Comparison

The British, German and Swedish codes do not state how often the board should meet while the Spanish code recommends meetings to be held periodically with a guideline of once a month.

	United Kingdom	Germany	Spain	Sweden	Only
No recommendation	UK	Ger		Swe	
Periodically			Esp		

Table 5:5 ***Amount of meetings***

5.3.4.2 Conclusion

The conclusion is that according to the codes in United Kingdom, Germany and Sweden the companies can decide the amount of meetings to be held on their own and when they see it necessary while in Spain it seems important to give a guideline.

This is a part of the codes that can be united into a common because once a month is not a harsh guideline for the other countries to follow.

5.3.5 Age

In this part of our model we will compare the recommendations about the age of directors stated in each code and conclude if such recommendations can be united in one common code or not.

5.3.5.1 Comparison

The German code has stated that a recommendation has to be made by the company in the Articles of Association and that this recommendation from the company itself then should be followed. The Swedish code had an age limit of 70 years in the proposal of the code but it was removed before the approval of the code.

	United Kingdom	Germany	Spain	Sweden	Only
No recommendation	UK		Spa	Swe	
Specified		Ger			Ger

Table5:6 ***Age***

5.3.5.2 Conclusion

The German code recommends the companies to decide the age limit on their own and the other codes do not give recommendations of a certain age. This part will not be difficult to unite in one common code, since a specific age is not recommended in the codes.

5.3.6 Term limits for directors

In this part of our model we will compare the recommendations about election and re-election of directors stated in each code and conclude if such recommendations can be united in one common code or not.

5.3.6.1 Comparison

The British code states that a re- election of all members of the board should be done every third year. A rigorous review shall be done before re-electing non- executive directors after six years and after nine years re-election of non- executives should be done every year. All such elections have to be made at the shareholders' meeting.

The Swedish code states that election and re-election of board members shall be done every year at the shareholders' meeting. When new directors have not been elected, the nomination committee (explanation further down) has to motivate why at the shareholders' meeting.

	United Kingdom	**Germany**	**Spain**	**Sweden**	**Only**
Re- election	UK			Swe	
Annually				Swe	Swe
Three years (all directors)	UK				UK
Review after 6 years (non-executives)	UK				UK
Annual re- election of non-executives after 9 years	UK				UK
No recommendation		Ger	Spa		

Table 5:7 ***Term limits***

5.3.6.2 Conclusion

Re- election of board members is stated as important in the British and the Swedish codes while in the other codes such recommendations are not mentioned.
The British code separates the rules between the executive and non- executive directors and points at the importance of the executives not to be a director for too long.

Since these differences exist, this part can be difficult to unite into a common code.

5.3.7 Chief executive officer (CEO)/ Chairman

In this part of our model we will compare the recommendations about if CEO and chairman should be represented by two different persons stated in each doe and conclude if such recommendations can be united in one common code or not.

5.3.7.1 Comparison

The British and Swedish codes recommend the chief executive (CEO) officer and the chairman to be two different persons.
Because of the two- tier board system in Germany the chairman of the supervisory board (SB) and the chairman of the management board (MB) are separated.
The Spanish code does not separate the chairman and the CEO, who can be the same person in Spanish companies.

	United Kingdom	Germany	Spain	Sweden	Only
CEO and chief executive- not same person	UK			Swe	
Chairman SB and chairman MB are separated		Ger			Ger
CEO and chief executive- same person is OK			Spa		Spa

Table 5:8 ***CEO/Chairman***

5.3.7.2 Conclusion

Once again the Swedish code stresses the importance to divide board and management while according to the Spanish code this is not important. The Spanish code explains that this recommendation is missing because parting them can lead to that transmission of information can be hindered between management and the board, generate coordination costs and derive the companies of strong leadership.

Since the recommendations in the Spanish code deviate from the other codes, this part can be difficult to unite into one common code.

5.4 Committees

In our analysis model we have divided the recommendations about committees stated in the codes into; the recommendation of committees, the nomination committee, the remuneration committee, the audit committee and other committees. We will in this section compare each and one of the recommendations between the codes.

5.4.1 Recommendation of committees

In this part of our model we will compare the recommendations stated in each code about which committees companies should form and then conclude if such recommendations can be united in one common code or not.

5.4.1.1 Comparison

The British and the Swedish codes recommend the same committees to be formed by companies; the nomination committee, the remuneration committee and the audit- committee.

The German code only recommends the companies to form an audit committee and states that companies can set up other committees if they judge it necessary. The recommendation of a nomination committee and a remuneration committee is therefore missing.

The Spanish code has put the remuneration and the nomination committee together into a common committee and calls it remuneration and appointment committee and also recommends the audit committee. The Spanish code also recommends two more committees; the executive or delegated committee and the strategy and investment committee, but at the same time states that these are not obligatory.

	United Kingdom	**Germany**	**Spain**	**Sweden**	**Only**
Nomination	UK		Spa	Swe	
Remuneration	UK		Spa	Swe	
Audit	UK	Ger	Spa	Swe	
Executives or delegated			Spa		Spa
Strategy and investment			Spa		Spa

Table 5:9 ***Committees***

5.4.1.2 Conclusion

The German code does not judge the committees as important since it just recommends the audit committee.
The Spanish code judges the strategy and investment of companies to be of such importance to give a recommendation of an own committee to handle such questions.

This part can be difficult to unite because of that the German code is missing the nomination and remuneration committee, which are seen as important in the other countries.

5.4.2 Nomination committee

In this part of our model we will compare the recommendations stated in each code about the nomination committee and then come to the conclusion if such recommendations can be united in one common code or not.

5.4.2.1 Comparison

The British code recommends the nomination committee to be composed of a majority of independent non- executives, the other half can either be executives or non-executives. The chairman of the board can be the chairman of the committee but not when appointment of successor of the chairmanship is dealt with. How the members of the nomination committee are appointed is not stated. This committee is recommended to lead the process of board appointments and make recommendations to the board and to evaluate the skills, knowledge and experience existing in the board.

The Spanish code states that the board of directors should appoint the members of the nomination/ remuneration committee and that all members of such committee should be externals (independent and domanial directors as stated before), with the same composition as the board. An executive director cannot form part of the committee. The work of the committee is to propose directors and managers and their remuneration and then report this at the shareholders' meeting.

The Swedish code states that the nomination committee is created to support the shareholders' meeting when selecting directors. Therefore the nomination committee in Sweden is seen as an organ for the owners (the shareholders), which chooses the members of the committees on the shareholders' meeting. The Swedish code states a minimum number of members to be at least three persons and at the same time states that the majority of the members shall not be directors and none of the members shall be senior manager. The chairman of the board shall not be chairman of the committee and there shall not be representatives for other comparative companies. The recommendation for the work of this committee is to propose the chairman, the directors and the auditors and the remuneration complying to them and such proposal shall be presented in the calling to the shareholders' meeting and on the company's website and also be motivated at the shareholders' meeting. The names of the members shall be declared at least six month before the annual shareholders' meeting.

	United Kingdom	**Germany**	**Spain**	**Sweden**	**Only**
Appointment and remuneration			Spa		Spa
All externals			Spa		Spa
Nomination	UK			Swe	
Composition					
Majority independent	UK				UK
Majority not directors				Swe	Swe
Senior managers prohibited				Swe	Swe
Minimum members				Swe	Swe
Chairman = chairman of board or independent non- executive	UK				UK
Chairman-not chairman of board				Swe	Swe
Elected on shareholders' meeting				Swe	Swe
Appointed by board			Spa		Spa
Names published				Swe	Swe
Work					
Propose directors	UK		Spa	Swe	
Propose directors' remuneration			Spa	Swe	
Evaluate balance of skills, knowledge, experience of the board	UK				UK
Propose auditors and remuneration				Swe	Swe
Propose managers and remuneration			Spa		Spa
Report to shareholders' meeting			Spa	Swe	

Table 5:10 ***Nomination committee***

5.4.2.2 Conclusion

We judge that the recommendations of composition of the nomination committee contain the most significant differences. Therefore we do not analyse the different recommendations of the work made by this committee. The British code emphasizes the importance of independent directors to form part of the nomination committee while the Swedish code stresses the importance of the board consisting of less than half of directors and leaving the managers out of the committee. The Spanish code takes a position in the middle, stating that executives should be left out of the committee.

Our conclusion is that in the British and Spanish codes it is fully possible that the directors themselves make the appointments to the board while in Sweden this is not possible since directors shall be less than the half of the members of the committee.
The Swedish code goes a little bit further in its openness and states that the names of the members should be known. The Swedish code is the only code that states the minimum number of members to form part of the nomination committee. This depends on that the directors shall be less than half of the members. If there are three members; two has to be non-directors, if there are five members; three has to be non- directors, etc.

This is a part that can be difficult to unite in one common code since the German code has not recommended this part, the British code states the non- executives to be important members and the Swedish code states the owner to be important members and that the directors of the board rather should be closed out.

5.4.3 Remuneration committee

In this part of our model we will compare the recommendations stated in each code about the remuneration committee and then come to the conclusion if such recommendations can be united in one common code or not.

5.4.3.1 Comparison

According to the British code the remuneration committee should exist of at least three (in smaller companies, two) independent members and it is for the board to set up such committee. The work of the remuneration committee is to set the remuneration of the executives and the chairman of the board and recommend and monitor the remuneration of senior management. Other remunerations to directors and managers are to be discussed with the chairman and the chief executive officer (CEO).

The Spanish code has united this committee with the aforementioned nomination committee.

Also in the Swedish code it is for the board to set up such committee. The chairman of the board can form part of the committee and also be the chairman of the committee. The rest of the members shall be independent to the company and senior management but not to owners. In the Swedish code the committee should prepare and propose remuneration and working conditions for senior managers. A special rule stated in the Swedish code is that in smaller companies the board can do the work of this committee but then a senior manager cannot participate in the work of remuneration. Smaller companies (with smaller board)[4] do not have to form such a committee.

	United Kingdom	Germany	Spain	Sweden	Only
Remuneration committee	UK		Spa	Swe	
Composition					
At least 3 independent non-executives (smaller companies - 2)	UK				UK
All independent to senior management and company				Swe	Swe
Chairman of board can be chairman				Swe	Swe
Established by board	UK			Swe	
Smaller companies, not needed (not manager)				Swe	Swe
Work					
Set remuneration to executives and chairman of board	UK				UK
Recommends remuneration to senior management	UK		Spa	Swe	
Recommends remuneration to directors			Spa		Spa
Consult chairman and CEO about remuneration to other directors and managers	UK				UK

Table 5:11 ***Remuneration committee***

5.4.3.2 Conclusion

According to the British code it is important that the committee is formed by independent members and the CEO can even be included in the process of remuneration, although not when deciding own pay. The Spanish code has made it possible for owners or owners' representatives to form part of such committee.
The Swedish code emphasizes the importance of that managers is left out of the committee while the owners are welcome to join.

This is an area that can also be hard to unite because the differences in composition of the committee where the British code recommends the members to be independent while the Swedish and Spanish code recommends the members to be owners.

[4] Six to seven members (Interview 2004).

5.4.4 The Audit committee

In this part of our model we will compare the recommendations stated in each code about the audit committee and then come to the conclusion if such recommendations can be united in one common code or not.

5.4.4.1 Comparison

The British code states the minimum amount of members of the audit committee to be three persons (in smaller companies, two), which should all be independent non- executive directors.
The recommended work of the committee is to monitor the financial statements and any formal announcement relating to the company's financial performance and that it should review the company's internal control and risk management. The committee should also make recommendations to the board about the appointment, re-appointment and removal of the external auditor and about the level of his/ her remuneration and review and monitor the independence and objectivity of the external auditors with the consideration of relevant British professional and regulatory requirements. The committee should also develop and implement policies regulating the supply of non-audit services from external auditors and review arrangements by which the staff of the company in confidence raise about possible improprieties in matter of financial reporting or other matters.

The German code states that members of an audit committee shall not be former members of the management board (MB) or the chairman of the supervisory board (SB). Therefore the members can be directors of the SB at the same time.
The recommendation of the work of the committee is that it shall handle issues of accounting, risk management and the necessary independence required for the auditor, audit mandate, auditing main points and the fee agreements.

According to the Spanish code the committee should only exist of external directors and the chairman should be an independent member.
The code recommends that the work of the committee should be settled in a special regulation, which should be approved by the board. The regulation should regulate how the committee should express its opinion on the annual, the quarterly and half-quarterly accounts, the handling of the internal control- systems and the monitoring of the internal auditing. The committee must also inform the board about changes in accounting criteria.
The committee should also express its opinion about selection, appointment, reappointment, remuneration and removal of internal audit manager and external auditors. The Spanish code also states that the work of this committee is Law- regulated (The law of measures to reform the financial system, article 47 of law 44/2002).

The Swedish codes states the minimum of members of the audit committee to be at least three directors. The majority of the directors shall be independent to the management and the company and at least one shall be independent to major owners. A director that forms part of management cannot form part of this committee. In companies with smaller boards this committee is not obligatory and the board can handle such work although then a manager sitting on the board cannot form part.
The recommendation of the work of the committee is that it shall ensure the quality of the financial reports, continually meet auditors and to monitor their work and discuss the co-operation between the external and internal auditors and review the company's risks. The

committee shall also set up guidelines of non-audit services that the external auditor contribute with and evaluate audit work and give proposals of auditors and their remuneration to the nomination committee.

	United Kingdom	**Germany**	**Spain**	**Sweden**	**Only**
Audit committee	UK	Ger	Spa	Swe	
Composition					
At least 3 independent non-executives	UK				UK
At least 3 board members				Swe	Swe
Manager can not form part				Swe	Swe
Majority independent to company and senior management				Swe	Swe
1 independent to major shareholders				Swe	Swe
All externals			Spa		Spa
Chairman independent director			Spa		Spa
Not former member of MB or present of SB		Ger			Ger
Work					
Monitor financial statements	UK		Spa	Swe	
Review internal control	UK	Ger	Spa		
Review auditing	UK	Ger	Spa	Swe	
Review risk	UK	Ger		Swe	
External/internal audit issues (independence, appointment, removal)	UK	Ger	Spa	Swe	
Non- audit services	UK		Spa	Swe	

Table 5:12 ***Audit committee***

5.4.4.2 Conclusion

This committee is recommended in all the codes but the recommendations, especially about the composition of the committee, are different. The British code recommends that all members should be independent. The independence criteria, even to owners is also stated in the Swedish code, but still it is more important that the independence is to managers and that others, for example owner can form part. Also the Spanish code judge it to be equally important that owners form part like independent members. The German code does not judge independence to be important at all.

Since there are so big differences in the recommendations about the composition of the board this part will be difficult to unite in a common code.

5.4.5 Other committees

In this part of our model we will compare the recommendations stated in the codes about special committees and then come to the conclusion if such recommendations can be united in one common code or not.

5.4.5.1 Comparison

The Spanish code recommends an executive or delegated committee with a similar composition as the board. This committee should support the board and managing the same work. According to the code this committee is not obligatory.

A strategy and investment committee is also recommended in the Spanish code that should inform and make proposals to the board about strategic decisions, investment and divestment. Executives and external members can compose the committee. According to the code this committee is not obligatory either.

	United Kingdom	Germany	Spain	Sweden	Only
Executive or delegated committee			Spa		Spa
Strategy and investment committee			Spa		Spa

Table 5:13 ***Other committees***

5.7.5.2 Conclusion

The Spanish code recommends these two committees but at the same time states them to be voluntary. The other codes have not recommended them but have all stated that other committees can be formed if necessary.

This part is possible to unite because the recommendations in the Spanish code are not obligatory and the other codes have mentioned that they can be made if necessary.

5.5 Remuneration

In this part, called remuneration we will compare the different recommendations of remuneration stated in each code to come to the conclusion is such recommendations are possible to unite in one common code or not.

5.5.1.1 Comparison

The British code has divided the recommendations of remuneration for directors into two parts; remuneration for executive directors and remuneration for non- executive directors. The code also contains a special part about how to design performance related remuneration for all directors.

The code states that remuneration to executive directors should contain a significant proportion of performance-based pay and states that stock-option programs should not be offered at a discount save.

The remuneration for non- executives should reflect the time commitment and the responsibilities of the role and should not include stock- options. If stock- options are included it should be approved by shareholders' meeting and should be held until at least one year after leaving the board. The remuneration for non- executive independent directors should not include incentive programs (for example stock- options).

A special part of the British code is called provisions on the design of performance related remuneration and contains guidelines for directors pay such as directors' annual bonus which should be designed to enhance shareholder value. It also contains recommendations about payments under long- term incentive schemes that should not be exercised before three years have passed and that should form part of a well considered over all plan and should be based on performance criteria reflecting the company's objectives. Such key variables of performance should be compared with a group of comparator companies and only basic salary should be pensionable.

The German code has divided the remuneration into two parts; remuneration for the management board (MB) and remuneration for the supervisory board (SB).

According to the German code the SB determines compensation for the MB.
To decide appropriate compensation the SB shall consider the task of the member of the MB, his/her personal performance, the MB's total performance and the company's economic situation, performance and outlook. The code recommends the compensation of the MB to be comprised of fixed and variable compensation where the variable compensation should be one- time annually payable components linked to the business performance or long- term incentives, for example stock options or comparable instruments with long-term incentive effect.

The shareholders' meeting or articles of association decides on the compensation of the SB. To decide the compensation of the SB the responsibilities and scope of task of the members of SB, the economic situation and performance of the company, the exercising of the chair and deputy chair positions in SB and the chair and membership of the committees are taken into account. The remuneration of the SB shall be comprised of a fixed salary and a performance- based compensation, which should contain components based on the long- term performance of the company.

The remuneration of the German boards should be compared with other comparative companies.

The Spanish code has divided the remuneration between directors and senior management.
The code recommends that remuneration referenced to the financial market (for example, shares and stock- options) should be limited to executive or internal directors.
It is recommended that the remuneration of each director is shown and divided into the parts that correspond to them including the delivery and assignment of shares, stock options or

systems referenced to the share- price, which all must be approved by the shareholders' meeting.
The code also states that the remuneration of senior management should be disclosed in the annual report, with a breakdown in salary in cash, stock options, bonuses, pension funds, provisions and other compensations. Golden handshakes or other protection clauses to senior management is self-regulated by the company but should have the approval of the board of directors.

The Swedish code has also divided the remuneration between directors and senior management when directors shall not receive such a pay appointed directly to senior managers or other employees and even if a CEO is a board member he/she cannot receive incentive pay appointed to the directors.
The remuneration to senior management has to be motivated and explained to shareholders' meeting. The explanation shall show the remuneration compared with performance, the main terms for bonus- and incentive programs, the main terms for non- monetary advantages such as pensions and golden handshakes and what circle of employees this comprehend.
The code finally states that the shareholders' meeting is to approve the remuneration to directors, chairman and members of the committees.

	United Kingdom	**Germany**	**Spain**	**Sweden**	**Only**
Remuneration	UK	Ger	Spa	Swe	
Directors	UK	Ger	Spa	Swe	
Executive/internal directors (incentive pay)	UK		Spa		
Non- executive directors (preferably not incentive pay)	UK				UK
Non- executive independent directors (not incentive pay)	UK				UK
MB/SB (incentive pay)		Ger			Ger
Senior Management		Ger	Spa	Swe	
Approved by shareholders' meeting	UK	Ger	Spa	Swe	
Criteria for remuneration	UK	Ger			

Table 5:14 ***Remuneration***

5.5.1.2 Conclusion

The British and the Spanish codes emphasize the importance to divide the remuneration between internal directors and external directors (non- executive, non- executive independent) and state that the external directors should not receive incentive pay such as stock- options. The British code further states the importance that incentive pay should be designed to enhance shareholder value. The German and Swedish codes do not contain this recommendation.

The German code recommends companies to divide remuneration between directors of management board and supervisory board.

The Spanish code also emphasizes that the transparency (the reporting of each remuneration) is more important than to recommend special rules of the composition of the remuneration.

The Swedish code stresses the importance not to give the same remuneration to directors and senior managers.

Since the codes recommend different directors and different remuneration to such directors this part can be hard to unite in a common code.

5.6 Shareholders' meeting

In this part, called shareholders' meeting we will compare the different recommendations about shareholders' meeting stated in each code to come to the conclusion is such recommendations are possible to unite in one common code or not.

5.6.1.1 Comparison

The British code states that a notice and related papers has to be sent to shareholders twenty working days before the meeting (approximately four weeks).
A company is recommended to communicate with the shareholders and understand their opinions and the code recommends special advantages for major shareholders for example that they have the opportunity to meet non- executive directors and discuss governance and strategy with the chairman. The code also states the importance of institutional shareholders and that such shareholders should have a dialog with the company. The code contains special principles that the institutional investors should apply, stating that such shareholders have a responsibility to make considered use of their votes.
According to the British code all directors should attend the shareholders' meeting and the chairmen of the committees should also be available to answer questions on the meeting.
Proxies can also be used to vote at a shareholders' meeting.

The German code does not state how far in advance the information about the meeting shall be sent to shareholders but states that shareholders are entitled to submit relevant questions and proposals before the shareholders' meeting and that information about the meeting should be available through electronic channels. It should be possible for shareholders to follow the shareholders' meeting on distance and information should be sent to foreign as well as to domestic shareholders.

According to the German code one share is one vote. This means that there are no shares with multiple voting rights, preferential voting rights (golden shares) or maximum voting rights.
The code also states that proxies can be used on the shareholders' meeting.

The German code also contains recommendations about what should be brought up at the meeting for example: net income and discharge for management board (MB) and supervisory board (SB), the election of shareholders' representatives and auditors. The meeting should also resolve separate issues like change of articles of association and changes of essential corporate measures.
In the German code MB should convene an extra ordinary shareholders' meeting in the case of takeovers. In this meeting the shareholders discuss the takeover and may decide on corporate actions.

The Spanish code states that the notice of the meeting should be disclosed sufficiently in advance and information should be available on the website and that information given to shareholders should be made easy to understand and be relevant.
According to the code it should be especially easy for institutional shareholders to attend the shareholders' meeting and also recommends that the institutional shareholders should disclose and define their policy of participation in the decisions of the company both to the company and to their investors.
The code further states that each company must set up a shareholders' meeting regulation, which shall be approved by shareholders' meeting. Such regulation should regulate the convening, preparation, notification, conduct (chair, answers to questions, duration, order, number of speakers, attendance, intervention and format of minutes) and exercising of political rights. The company can decide the content of each rule treated in the regulation, but then has to follow these rules.
The removal of specific officers or protective measures aimed at preventing takeovers should be approved at the shareholders' meeting.
Shareholders with conflict of interest should not vote on the meeting.
The code also states that proxies can be used to vote at shareholders' meeting.

The Swedish code states that the time and place for the ordinary meeting shall be exposed six month in advance and it should also be exposed on the website and also states that information about an extra meeting shall be exposed as soon as possible before the meeting. Information given to shareholders shall be relevant and easy to understand. According to the code a company shall consider the possibility to hold the shareholders' meeting in other languages or make the information available in other languages. The code also recommends the possibility for shareholders to participate and follow shareholders' meeting on distance and states that shareholders can give notice through e-mail if they are going to attend the meeting. According to the code, companies shall also inform the shareholders about how they can make suggestions and to whom they can make them.

According to the Swedish code the directors, the CEO and one auditor of the company have to participate the shareholders' meeting, while members of committees can participate if they have suggestions on errands. Managers shall participate if necessary. If an extra meeting is held the code states that there should be sufficient presence of directors to make decisions.
A chairman of the shareholders' meeting has to be appointed and cannot be a director, an adjusting person also has to be appointed and shall be shareholder or shareholder representative and cannot be a director.
It is only the Swedish code that states a majority of votes is necessary for a decision to be made at the shareholders' meeting.

	United Kingdom	Germany	Spain	Sweden	Only
Calling for the meeting					
Time and place exposed				Swe	Swe
6 months in advance				Swe	Swe
20 working days in advance	UK				UK
Sufficiently in advance			Spa		Spa
Shareholders' rights					
Communication with shareholders and their opinion important	UK				UK
Shareholder entitled to submit relevant questions and proposals		Ger			Ger
Explain to whom and how shareholder suggestions can come to be treated				Swe	Swe
Special advantages for major shareholders	UK				UK
Special rules for institutional shareholders	UK		Spa		
Information					
Easy to understand & relevant information			Spa	Swe	
What kind of information to shareholders	UK	Ger			
Use modern technology		Ger	Spa	Swe	
Participation on distance		Ger		Swe	
Information on the website		Ger	Spa	Swe	
Participation					
All directors should attend	UK			Swe	
Chairmen of committees	UK			Swe	
CEO				Swe	Swe
Auditor				Swe	Swe
Appoint chairman of the meeting (not director)				Swe	Swe
Adjusting person appointed (shareholders representative, not director)				Swe	Swe
Shareholders' meeting regulation			Spa		Spa
Voting					
Majority of votes for the decision					
One share = one vote		Ger			Ger
Proxies	UK	Ger	Spa		
Takeovers		Ger	Spa		
Foreign shareholders taken into consideration		Ger		Swe	

Table 5:15 ***Shareholders' meeting***

5.6.1.2 Conclusion

The British code points at the importance of communication with the large shareholders and also states the importance for the institutional shareholders to make use of their votes.

Both the British and Spanish codes judge it important to have a special regulation for institutional investors.
The German code has clearly stated the one share, one vote principle while the Swedish code stresses the importance of majority voting at the shareholder' meeting.
All codes, except the Swedish state that proxies can be used to vote.
According to the Swedish code it is important that members of board, management and auditors are present at the shareholders' meeting.

This part will be hard to unite in one common code because of the many differences. For example the one share, one vote principle, the recommendations about special regulations of institutional shareholders.

5.7 Reports

In this part, called reports we will compare the different recommendations of reports stated in each of the codes to come to the conclusion if such recommendations are possible to unite in one common code.

5.7.1.1 Comparison

The British code recommends companies to make a corporate governance report. The company should also state how it applies the recommendations in the code according to the comply and explain principle (stated above). The report should be available on request on the company's website.

The German code does not state a recommendation about that a company has to make a corporate governance report. It just states that financial reports have to be made.

The Spanish code states that a company should make a corporate governance report that should be available on the company's website. The code also recommends a public disclosure of a company's owner structure (powers within the company, capital structures, percentage of significant shareholdings and families) and the management structure (identity, track record, stake in the company, remuneration, functions and post held, relationships, cross-directorships, appointment, removal and re-election of managers and directors), related party and intra group transactions (reporting on transactions between company and its core shareholders, directors and senior managers), risk control systems (the assessing, mitigation or reduction of company risks) and the functioning of the shareholders' meeting (the shareholders' meeting regulation mentioned before).

According to the Swedish code the company shall make a special report on corporate governance and the auditor of the company shall review this report.
In the corporate governance report the company shall state how the code is followed and name the rules the company does not follow and explain why.
A report of internal control shall be made by the board and reviewed by the auditor who also shall make a statement on the report. All this shall be put in the annual report together with the financial statements of the company.
A special part of the company's website shall contain the information about corporate governance.

Reports	United Kingdom	Germany	Spain	Sweden	Only
Corporate governance report	UK		Esp	Swe	
Other reports			Esp	Swe	
Available on website	UK		Esp	Swe	

Table 5:16: ***Reports***

5.7.1.2 Conclusion

The German code does not judge a corporate governance report to be important while the other codes do. The Spanish code also states the importance of making other important information available to the financial markets and especially stresses the importance to show the owners and their influence on the company, this part is not stated by any of the other codes.

This part can be easy to unite in one common code, while the British, Spanish and Swedish code state that a corporate governance report should be made. Although the German code does not give such a recommendation one can imagine that the companies make such reports although its not recommended.

5.8 Summary of all conclusions

The comply or explain principle is the basic tool for self-regulation in all the codes. Since this recommendations of this principle are similar in all the codes this part can be united in a common code.

The part called duty of loyalty, duty of diligence and the conflict of interest is differently stated in each code although we conclude that the main difference lies in the different recommendations of in which interest directors should work. To begin with the British code recommends directors to work in the best interest of shareholders while the German and Spanish codes recommend the work to be done in the best interest of the company. The Swedish code recommends directors to work in the best interest of both the company and the owners.
Therefore the recommendation for duty of loyalty, duty of diligence and conflict of interest is difficult to unite in one common code.

The recommendations for the composition of the board are differently stated in the codes since the British code points at the importance of independence to both company and owners while the Swedish and Spanish codes recommend owners to form part of the board and the German code is missing such recommendations. The Swedish code rather points at the importance of keeping management out of the board. The recommendations of different board structures (one- tier and two- tier board) also differ between the codes.
The Swedish code has also recommended the board to be composed by an equal proportion of men and women.
All these differences in the recommendations make this part difficult to unite in one common code.

The biggest difference in the independence criterion is that the German code is totally missing this recommendation. Further the British code recommends that to be independent, the directors should not receive incentive pay. This recommendation is missing in the other codes. There is also a difference between the recommendations about interlocking- directorship in the codes since the British code states that independent directors should not form part of more than one board, the Spanish code recommends that independent directors do not form part of an owner's board if that owner has a domanial director forming part of the first board. The Swedish code rather points out the importance of that management is not having influence of the board when stating that senior managers of other companies not can form part of the first company's board if the first company has managers as directors forming part of that board.
Because of all these differences in the recommendations about independence between the codes, such recommendations will be difficult to unite in one common code.

The recommendations about the size of the board differ between the codes somewhat since the British, Spanish and Swedish codes point at the importance for the board to be effective in its work and therefore not to be too large and the German code points at the importance for a company to decide on its own. The recommendations are not that different that they will be difficult to unite in one common code.

The recommendations in the codes about the amount of meetings can be put together in a common code since the codes do not differ in these recommendations. Although the Spanish code recommends meeting to be held once a month this recommendation is not that harsh to make it impossible to unite in one common code.

The German code recommends the companies to decide the age limit on their own and the other codes do not give recommendations of a certain age. This part will not be difficult to unite in one common code, since a specific age is not recommended in the codes.

The recommendations of the re- election of board members are only stated in the British and Swedish codes therefore such recommendations can be hard to unite in one common code.

The Spanish code is missing a recommendation about dividing chief executive officer and chairman therefore this recommendation can be difficult to put in one common code.

The German code only recommends the formation of an audit committee therefore it will be difficult to put recommendations about which committees to form, in one common code.

In the Spanish code the nomination committee and the remuneration committee are put together into one common committee called remuneration- and appointment committee.
The composition of the nomination committee is differently recommended in all the codes. The British code recommends a majority of independent directors. The Swedish code recommends that managers should be left out and that the majority should not be directors. Finally the Spanish code recommends that executives do not form part of the nomination committee. Because there are big differences in the recommendations about the composition of the nomination committee it will be difficult to unite such recommendations in one common code.

Recommendations about composition of remuneration committee are also differently recommended since the British code recommends independent members to form part, while the Spanish code makes it possible for owners to form part of the committee. Finally the Swedish code recommends that managers are left out and owners are welcomed. Therefore we judge this recommendation to be difficult to unite in one common code.

The Spanish code recommends two extra committees, which are voluntary; the executive or delegated committee and the strategy and investment committee. We have not found a reason for the other codes not to recommend these committees and since they are not stated to be obligatory in the Spanish the other codes could also recommend such committees.

The only committee recommended by all the codes is the audit committee but the recommended composition is different between the codes since the Spanish and Swedish codes judge it more important for the owner to form part while the British code emphasizes the importance that the committee is composed by independent members and the Swedish code points at the importance of not let managers form part. Therefore these recommendations will be hard to unite in one common code.

The recommendations about the remuneration differs between the countries since the British code parts the remuneration between the executive directors, non- executive directors and non- executive independent directors while the Swedish code states the importance of that directors not get the same pay as management. The German code divides remuneration between management board and supervisory board. The Spanish code recommends companies to decide the remuneration on their own but the remuneration should be clearly showed (transparency).

The recommendations about the shareholders' meeting is hard to unite in one common code since the German code recommends the principle of one share, one vote and the British and Spanish codes state the importance to have a special contact with institutional and major shareholders and the German code does not emphasize the importance to call for the meeting in advance. The Swedish code emphasises the importance of directors, chairmen of committees, CEO and auditor to be present at the meeting.
Because of all these differences in the recommendation a single, common recommendation will be difficult to form.

The recommendations about the reports can be easy to put in a common code since the British, Spanish and Swedish codes recommended and although not stated in the German code one can conclude that the companies are to show their compliance through some kind of report.

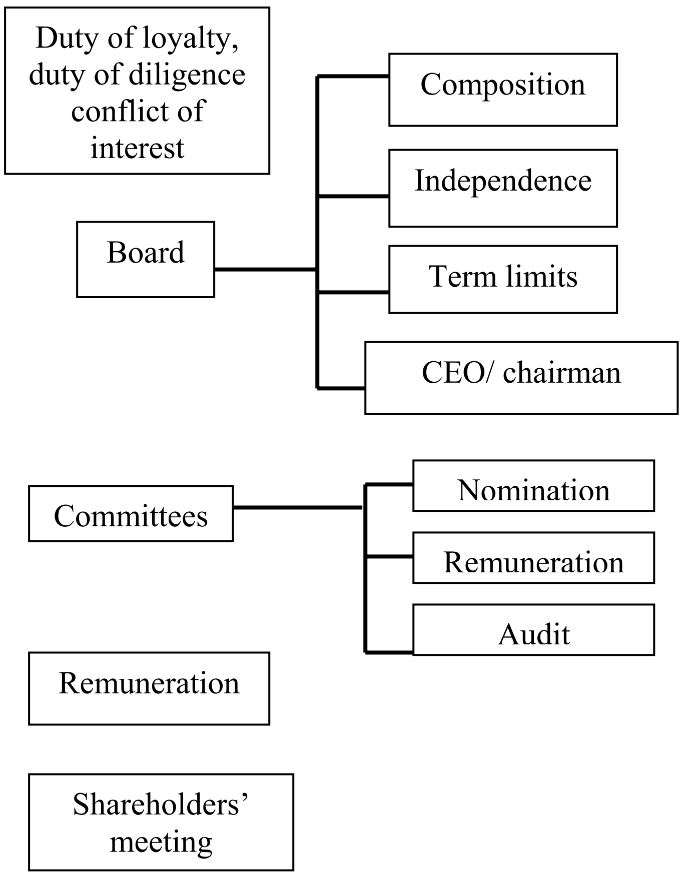
5.9 Non-compatible parts

Throughout our formal analysis we have come to the conclusion that there are recommendations in the codes that cannot be united in one common code. We have also concluded that there are parts that are possible to unite.

The parts in our analysis model that are hard to unite because of the different recommendations stated in the codes are; duty of loyalty/duty of diligence and conflict of interest, composition of the board, independence criteria of the board, term-limits, chief executive officer (CEO)/chairman, proposed committees, nomination committee, remuneration committee, audit committee, remuneration and shareholders' meeting.

To make it easier to understand which parts of our model that are hard to unite it will be illustrated by the following picture (*picture 5:6*).

Non-compatible parts



Picture 5:6

These are the non- compatible parts (the parts that contains recommendations difficult to unite) according to our formal analysis. The next step in our research is now to move on to our next analysis, called the institutional analysis and look into if the differences in the recommendations of the codes are built on the institutional systems existing in each country.

6. Introduction to the institutional systems

In this chapter we will briefly introduce the main characteristics of the different institutional systems (Anglo-Saxon, Germanic and Latin) existing in Europe. These are the main institutional systems existing in Europe and represent the institutional systems existing in United Kingdom, Germany and Spain. The Swedish institutional system lies in between these main systems.

6.1 The Anglo- Saxon institutional system

According to Weimar and Pape (1999) the Anglo- Saxon institutional system entails, in Europe, the United Kingdom.

The Anglo- Saxon system is characterized by a dispersed ownership of companies (Bratton and McCahery 2002).

According to Coffee (2002) the Anglo- Saxon system is also characterised by high disclosure standards and high market transparency.

According to Aguilera and Jackson (2003) the Anglo- Saxon system is further characterized by that households invest in companies' stocks and bonds, thereby expanding the size and liquidity of capital markets and leaving the primary monitoring role to institutional investors and other shareholders instead of banks. In this system shareholders have control over the firms by having option to exit (to sell their shares) if the firm no longer fulfils their interest.

According to Franks and Mayer (1990; cited by Weimar and Pape 1999) the stock- market plays an important role in the Anglo-Saxon countries and such countries are also known for their active external markets for corporate control (take-over market). The market for corporate control functions like a protection for shareholders where managers manage the companies under the threat of being exchanged if shareholders are not satisfied.

The companies in the Anglo- Saxon system are often characterized as conceived as a combination of managerial directors, which are working for the best interest of shareholders – to create shareholder value, and the law in Anglo-Saxon countries strongly protects shareholders (Weimar and Pape 1999).

The one- tier board structure is also characteristic for countries of the Anglo- Saxon system and the boards contain executive- and non- executive directors, where the non- executive directors work primarily in the best interest of the shareholders (Lorsch and McIver 1989; cited by Weimar and Pape 1999).

In the context of corporate governance, executive compensation is often aligned with the performance on the firm and common remuneration, like stock- options, are often set to align the management interest with the interest of shareholders (Weimar and Pape 1999).

6.2 The Germanic institutional system

According to Weimar and Pape (1999) the Germanic system entails Germany, the Netherlands, Switzerland, Sweden, Austria, Denmark, Norway and Finland in the Europe.

According to Bratton and McCahery (2002) the Germanic system is characterized by majority or near- majority holdings of stock held by one, two or small groups of large investors. In Europe, the largest investors tend to be individuals or rich families, with non-financial firms and banks making a secondary appearance in countries like Germany and Sweden. In these kinds of systems the large shareholders have a closer monitoring function and are more informed than in systems characterized by a dispersed ownership such as United Kingdom.

According to Aguilera and Jackson (2003) the Germanic system is characterized by that the control of the firms is closely related to capital and the banks are the key financial institutions, mediating deposits from households and channelling them into loans made directly to firms. Such systems tend to have small and underdeveloped capital markets and that the firms in such markets are more dependent on debt and financing through bank loans.

Companies existing in Germanic systems are often seen as a coalition of various participant, such as shareholders, corporate management, employees, suppliers of goods and services and suppliers of debt, striving to work in the best interest of the firm as a whole (Moerland 1995 a; cited by Weimar and Pape 1999).

Some Germanic countries (like Germany and the Netherlands) often have a one- tier structure of the companies' boards, but this is not the typical characteristic for all the countries in this kind of system (Weimar and Pape 1999).

The stock- market plays a less important role in the Germanic countries than in the Anglo-Saxon countries and an active market for corporate control is almost non- existent (Weimar and Pape 1999).

6.3 The Latin institutional system

According to Weimar and Pape (1999) the Latin system in Europe entails France, Italy, Spain and Belgium in the Europe.

The concept of companies in Latin countries lies in between the Germanic and the Anglo-Saxon institutional systems. The shareholder influence of firms is greater than in the Germanic countries but not as important as in Anglo- Saxon countries. (Weimar and Pape 1999).

According to Moerland (1995; cited by Weimar and Pape 1999) the Latin countries are characterized by cross- holdings, family control and a relatively high ownership concentration where the stock- market plays a much less important role than in the Anglo- Saxon countries. Furthermore an active market for corporate control is almost non- existent in Latin countries. (Weimar and Pape 1999).

7. The institutional analysis

In this chapter we will explain the different characteristics of the institutional systems existing in United Kingdom, Germany, Spain and Sweden. Finally we will, in a table, show the main features of each institutional system.

7.1 The British institutional system

7.1.1 The duty of loyalty and the conflict of interest

A characteristic of the British institutional system is that directors and senior managers manage the corporation in the interest of its shareholders and that other stakeholders such as creditors, employees, suppliers, and costumers, have their interest protected by contractual and regulatory means rather than through participation in corporate governance (Hansmann and Kraakman 2002). United Kingdom has an economy referred to as a shareholders' economy, therefore the aim for British companies is to maximise the profits for the investors (Bolkenstein; cited by Cheffins 2002).

According to Crespí, Gispert and Renneboog (2002) the ownership and control are separated (the owners do not manage the companies) in United Kingdom and therefore a conflict of interest can arise between managers' interest and shareholders' interest

7.1.2 The ownership structure

According to Goergen and Renneboog (2001), British listed companies tend to have a dispersed ownership structure. Therefore it is uncommon for British public companies to have a dominant shareholder since less than one- fifth of British publicly quoted firms have an owner who owns more than 25 per cent of the shares (Berglöf 1997; Davies 1998; and Wymeersch 1998; cited by Roe 2002).

The British companies are controlled by insider shareholders that are managers and directors due to the fact that in British companies the members of the controlling organs such as managers and directors own shares of the company. Such share- ownership can influence managers and directors in two ways; it could lead to an incentive to work towards share- price maximising strategies or it could lead to expropriation of minority shareholders. (Goergen and Renneboog 2001).

The largest category of investors in United Kingdom are institutional shareholders. Studies show that these investors are not involved in corporate monitoring because they find it easier and cheaper to sell their holdings, and they do not want to form part of the board for the fear of getting price sensitive information. Therefore, despite the size of their holdings, they are not known for their monitoring function and hardly for voting on the annual meetings (NAPF 1996; cited in Faccio and Lasfer 2002). As a result there are concerns in United Kingdom about how to monitor such institutional shareholders (Maher and Andersson 2002).

The size of the largest ultimate outside voting block for listed industrial companies in the United Kingdom is 9.9 %, while, in Germany it exceeds 50 % and in Spain it is 34.2 % (Becht and Roell 1999; cited by Cuervo 2002). These figures show that United Kingdom is characterized by a dispersed ownership.

The family controlled companies in the United Kingdom is least occurring in comparison with other European countries according to Faccio and Lang (2000; cited by Thim and Åkerberg 2003).

According to La Porta, Lopez-de-Silanes, Shleifer and Vishny (1999; cited by Thim & Åkerberg 2003) the British banks are strong, since they are allowed to own majority share. On the other hand Thim and Åkerberg (2003) are of the opposite opinion; that banks are weak since they neither contributes to external capital or stand as owners to companies. Köke and Renneboog (2003; cited by Thim and Åkerberg) emphasize the fact that it is unusual that banks have controlling voting rights in companies.

In the British financial market, households invest in companies' stocks and bonds, thereby expanding the size and liquidity of capital markets and leaving the primary monitoring role to institutional investors and shareholders instead of banks. The control function of the shareholders is that they have the option to exit (sell their shares) if the firm no longer fulfils their interest. (Aguilera and Jackson, 2003).

7.1.3 Pyramidal structures, cross- holdings and dual- class shares

In United Kingdom the principle of "one share, one vote" is applied (Weimar and Pape 1999). Shares with different voting rights are legal in United Kingdom but British firms tend to avoid them because it has been discouraged by institutional shareholders as well as in the Stock Exchange rules (Goergen and Renneboog 2001).

7.1.4 Proxies

Proxies can be used in United Kingdom and are normally exercised by company directors and thus confer additional power to these (Goergen and Renneboog 2001).

7.1.5 Performance based pay

Incentive arrangement for managerial remuneration might be expected in the dipersed market economy existing in United Kingdom because of the weak incentive for any individual shareholder to incur the costs of monitoring management (Carlin and Mayer 2002).
According to Crespí-Claders and García-Cestona (2002) the compensation to managers are tied to corporate performance to align the interest of the shareholders and managers in United Kingdom but such compensation plans geared to align the interest of managers with those of shareholders can lead to short- term behaviour. For example, when managerial remuneration is due largely to stocks or stock options, managers have an incentive to maximize short- term results in order to increase their own compensation. The same problem can occur when directors get such pay. (Maher and Andersson 2002).

7.1.6 Take-overs

The British system is characterised by an active external market for corporate control, often referred to as the takeover market where the most used takeover techniques are mergers, tender offers, proxy fights and leveraged buyouts (Frank and Mayer 1990; cited by Weimar and Pape 1999).
According to Weimar and Pape (1999) takeovers are regarded as a central function of the stock market in United Kingdom.

Maher and Andersson (2002) state that, in United Kingdom, there has been an average of over 200 mergers and acquisitions per year during the last decade, compared with an average of about 50 in Germany.

Take-overs are supposed to have a disciplinary role for managers to work in the best interest of shareholders but two empirical studies questioned the disciplining role of take-overs in United Kingdom and found that there was no significant difference from that of targets of friendly bids or non- targets and that managers are generally free to do what they choose since disciplining of poor management does not work effectively. (Frank and Mayers 1996; cited by Goergen and Renneboog 2001).

7.1.7 Minority Protection

United Kingdom is known for its strong protection of minority shareholders (Goergen and Renneboog 2001) and non- controlling shareholders receive strong protection against controlling shareholders (Hansmann and Reiner Kraakman 2002).

La Porta et al (1997; cited by Bratton and McCahery) found that investors are well protected in English common law, somewhat protected in German and Scandinavian common law and are most vulnerable in countries of French origin.

7.1.8 Composition of the board

The British companies have a one- tier board structure, in which, executives and non-executives form part (Goergen and Renneboog 2001).
The non- executive members are external experts, who also can be executive board members of other firms. These external directors are responsible for the management of the corporation, and are expected to exercise the duties of loyalty, care and good business judgement, and their primary accountability is to shareholders. (Lorsch and MacIver 1989; cited by Weimar and Pape 1999).
Both the executive and non- executive board members are appointed and dismissed by the shareholders' meeting (Bleicher and Paul 1986; cited by Weimar and Pape 1999).

7.1.9 Independence of the board

In United Kingdom there is a strong emphasis on independent directors to form part of the board. Independence is particularly important when board members are responsible for overseeing the executive and board remuneration (Maher and Andersson 2002).
According to Melvin (2004) a large proportion of the non- executives of the board should be seen as independent. The final decision of if non- executives are independent lies with the shareholders that elects them.

7.1.10 The summary of the British institutional system

- The directors and the senior management work in the shareholders' interest.
- The stakeholders interest are protected by contracts and regulatory means.
- United Kingdom is a shareholder economy.
- British companies tend to have a dispersed ownership.
- Control lies with insider shareholders.
- In British companies managers and directors owns shares; this could led to incentives to share- price maximising strategies or exportation of minority shareholders.
- Institutional shareholders are the largest category of investors in United Kingdom, but are not known for monitoring and neither for voting at annual meeting.
- Shareholders controlling function is to sell their shares if not satisfied.
- The use of 'one share one vote' principle is applied.
- Use of proxies, usually carried out by company directors.
- To align the interest of shareholders and managers, some of the managers compensation are tied up to corporate performance.
- The British system is characterised by an external market for corporate control.
- Take-overs are supposed to have a disciplinary role, but are weaker than thought.
- The UK is known for strong protection for minority shareholders.
- The British companies have a one- tier board structure.
- There is a strong emphasis on independent directors to form part of the board.

7.2 The German institutional system

7.2.1 Duty of loyalty and the conflict of interest

In Germany firms are considered as a coalition of various stakeholders, such as shareholders, corporate management, employees, suppliers of goods and services, suppliers of debt and costumers (Moerland 1995; cited by Wiemar and Pape 1999). Therefore directors are supposed to work exclusively in the best interest of the company and as a consequence, the interest of the shareholders in Germany should only be pursued to the extent that it is not harmful to the interest of the company (Schilling 2001).

7.2.2 Ownership structure

According to Prowse (1995; cited by Weimar and Pape 1999) roughly one- quarter, in a sample of 310 listed non- financial German companies, had majority shareholders and therefore he came to the conclusion that the ownership concentration is significantly high in German companies.

According to Carlin and Mayer (2002) even the large quoted companies in general have at least one shareholder owing more than 25 per cent of equity. Cuervo (2002) states that large shareholders in Germany are Banks, companies and families.

The concentration of control is high in Germany due to large block- holders and proxies used by banks (Becht and Böhmer 2001).

In Germany banks exercise considerable authority (Charkham 1994; Macey and Miller; Scott 1997; Prigge 1998; cited by Cheffins 2002). This is due to the governance related functions the banks have in Germany (they function like advisors, lenders, owners of shares on their own behalf and the use of proxies given to them from other shareholders) (Cheffins 2002).

Furthermore the banks play a major role in firms, through equity stakes, proxies given to them by small investors and bankers' position on the boards of firms (Baums 1993; Kester 1997; cited by Cuervo 2002). Also, German banks are important sources of influence on the corporations; the credit- giving bank can have insight into the corporations, when the banks hold major participation in German corporations (Hopt 2002).

Thim and Åkerberg (2003) are of the opinion that banks are strong since they are the main providers of external capital to the German companies. They further state that banks in Germany are not the dominated owners as one might believe, it is only the fifth largest owner but the banks keep their control through proxies.

7.2.3 Pyramidal structures, cross- holdings and dual- class shares

According to Becht and Böhmer (2001) the one-share-one vote principle is used by listed companies in Germany.

Shares with different voting rights was used by 18 % of the German companies According to Bennedsen and Nielsen (2002; cited by Thim & Åkerberg, 2003). The research was based on 740 companies.

The German governance system is characterised by that non- financial corporations own 38 % of the shares of listed firms. Such mutual cross-shareholdings between firms are generally permitted and commonplace and it is unusual for such companies to launch unwelcome takeovers (Franks and Mayer 1990; cited by Weimar and Pape 1999). Germany also has strong laws treating cross- ownership (La Porta et al 1999; cited by Thim and Åkerberg 2003).

Pyramid structure is also used according to Frank and Mayers (2001; cited by Thim and Åkerberg 2003). The research was based on 477 listed companies during 1989- 1994.

7.2.4 Proxies

Proxies can be used and are in Germany normally exercised by banks. If shareholder does not express his/her voting intentions a bank is free to vote as it pleases (Becht and Böhmer 2001) and it is common practice of shareholders in Germany to let the bank, which holds their shares in custody, vote with the shares in the general assembly. To do this, the bank must ask the client for a specific mandate to represent him/her and for instructions on how to vote. The bank must clearly state how to vote if it does not get such instructions and the law states that the bank must act only in the interest of the client. (Hopt 2002).
The banks often have a large proportion of the shareholders' voting rights (Gottschalk 1998; cited by Thim and Åkerberg 2003) and even if banks only owns a small block the proxy votes often gives the banks majority control (Becht and Böhmer 2001).

7.2.5 Performance- based pay

The use of performance- related compensation in Germanic countries is rather limited. But variable compensation is becoming more and more important in these countries. In Germany hardly any performance- related compensation was used according to Abowd and Bognanno (1995; cited by Weimer and Pape 1999)

7.2.6 Takeovers

Generally, in Germany, influence on managerial decision- making is not exerted via the "invisible hand" of stock- markets, but via the visible hand of dialogue between the management board and the supervisory board around the negotiation table. The ownership structure partly explains the absence of an active market for corporate control. The more concentrated markets are held, the more mechanisms shareholders can use effectively to influence managerial decision- making in a direct manner, and the less acute is the "option of last resort" to correct managerial decision- making by (the threat of) a hostile takeover. (Weimar and Pape 1999).

7.2.7 Minority Protection

The minority protection by law is very poor in Germany (Gugler and Yortoglu 2002; La Porta et al 1998; cited by Thim and Åkerberg 2003).

7.2.8 Composition of the board

The two- tier board structure has a management board (MB) and a supervisory board (SB).

The German corporate law mandates a two- tier board structure for stock corporations comprised of a management board (Vorstand) and a supervisory board (Aufsichsrat), which provide a separation between management and supervision of management (Weimar and Pape 1999).

The members of the supervisory board consist of shareholders, employees and banks (Thim and Åkerberg 2003).
According to Scheider- Lenné (1994; cited by Weimer and Pape 1999) the total number of supervisory boards' seats, 1 495, of the 100 largest German firms in 1988, 136 were occupied by representatives of banks, while 729 seats were appointed to trade unions and other employee representatives.

The control is exercised by the boards of directors with internal or external directors linked to large shareholders (Aguilera and Jackson 2003).

7.2.9 Stakeholder representatives

The stakeholder interest of the Germanic system appears in the board- room with employee representatives as directors where in corporations with 2 000 employees or more, one half of the Supervisory board's seats must be occupied by employee representatives (smaller companies have to appoint one- third) (Wymeersch 1998; Cunningham 1999; cited by Cheffins 2002).

The right of employees to participate in decision- making is known as codetermination. The other members of the supervisory board are appointed by the shareholders' meeting (Hauptversammlung), which also has the right to elect chairman, who has double voting rights (Weimar and Pape 1999).

There are representatives of banks on the supervisory boards of most large German companies and the "power" of the banks is founded both on direct participation – as shareholders – and on the fact that they hold shares on behalf of costumers and can exercise influence through the proxy voting rights assigned to them by these costumers (Gottschalk 1988; Perlitz and Seger 1994; cited by Reeves and Kelly- Holmes 1996).

7.2.10 Independence of the board

On the German supervisory boards there is a mandatory independence of management for all directors. The independence criteria is not like in United Kingdom, because in Germany the supervisory board- members are appointed because of the banking, business or other relationship he/she or his/her employer has with the corporation. (Schilling 2001).

The influence of individual shareholders on managerial decision- making in German companies is limited (Weimar and Pape 1999) and independent entrepreneurs are almost non-existent on the boards of the major German corporations (Schilling 2001).

7.2.11 The summary of the German institutional system

- The directors work is in the interest of the stakeholders.
- German companies are characterised by a concentrated ownership.
- Banks in Germany are not dominant owners, but keep control due to proxy.
- The one- share- one vote is used by important blockholders of listed companies in Germany.
- Other protective measures of ownership and control are; cross- ownership and pyramid structure.
- Performance based- pay hardly exists.
- Proxies are usually carried out by banks.
- Take-overs are not common practice.
- The minority protection is poor.
- Germany has a two tier- board structure; with SB and MB. Shareholders, employees and banks are represented in the SB.
- Independent entrepreneurs on the boards are almost non- existent.

7.3 The Spanish institutional system

7.3.1 Duty of loyalty and conflict of interest

Family firms existing in Spain apply a shareholder view since the foundations of the companies are based on shared values and long- term relationships (Carlock and Ward 2001; cited by Suáre and Santana-Martín 2004).

The potential conflict of interest in Spanish companies usually arise between large and minority shareholders, or between strong owner managers and minority shareholders (Shleifer and Vishny 1997; cited by Fernández-Rodríguez, Géomez-Ansón and Cuervo-García 2004).

7.3.2 Ownership structure

Spain is recognised by a concentrated ownership of firms and this can be illustrated by the fact that; the three largest shareholders hold 50 per cent of the firm's shares, in contrast the same figure in United Kingdom is around 20 per cent (La Porta et el 1999; cited by Fernández-Rodríguez et al 2004). Furthermore, the proportion of firms with no controlling shareholder[5] is 35 per cent for listed large companies and cero per cent for listed medium-size companies (García-Cestona 1998, Faccio and Lang 2002; cited by Fernández-Rodríguez et al 2004).

Family-ownership, cross-ownership, state-ownership and pyramidal structures are characterising Spanish firms (Moerland 1995; cited by Thim and Åkerberg 2003).

Banks, companies and families in Spain are large shareholders (Cuervo 2002). The majority of large shareholders are family groups (67 per cent) and widely held financial companies (15,07 per cent). According to different studies, families control between 40 per cent (Santana-Martín and Cabrera- Suárez 2001; cited by Suáre and Santana-Martín 2004) and 60 per cent (Faccio and Lang 2002; cited by Suáre and Santana-Martín 2004) of listed companies.

Furthermore, empirical results show that in most firms the Chief executive officer (CEO) is a family member and that the presence of other family members is around two (Suáre and Santana-Martin 2004). According to a company study; in 60 % of the companies the CEO, the board's Chairman or the Vice- Chairman are from controlling families. (Crespí 2002).
Also it is shown that the firms are almost entirely controlled by the family members and that the presence of non- family shareholders is insignificant (Suáre and Santana Martín 2004).

According to Crespí (2002), bank- ownership is generally small in Spain but different opinions about how strong banks are in Spain exist, on the one hand banks are considered strong since they can have a majority share in companies (La Porta et al 1999; cited by Thim and Åkerberg 2003) on the other hand the opinion is that banks are weak due to the fact that they neither contribute with external capital or represent ownership in Spanish firms (Thim and Åkerberg 2003).

[5] That is a shareholder whose voting rights exceeds 20 per cent

7.3.3 Pyramidal structures, cross- holdings and dual- class shares

Different voting powers were rarely used in Spain during 1996- 2000 (Faccio and Lang 2000; cited by Thim and Åkerberg 2003).

According to Crespí (2002) pyramidal and complex ownership structures have been created in Spanish corporations, via cross- holding companies and the Spanish corporate sector (industrial holding companies) owns a large stake in itself. Such cross-ownership is strongly law regulated in Spain (La Porta et al 1999; cited by Thim and Åkerberg 2003). Furthermore, studies made in Spain showed that the use of pyramid structures were medium/ high (La Porta et al 1997; cited by Thim and Åkerberg 2003).

7.3.4 Proxies

Proxies exist but companies can require that they only are given to other shareholders of the company (Baums 1998; cited by Thim and Åkerberg 2003).

7.3.5 Performance based pay

In the Latin Countries performance related pay generally do not exist (Weimer and Pape 1999).

7.3.6 Take-overs

According to Moerland (1995; cited by Thim and Åkerberg 2003) an active market for corporate control is missing in Spain and hostile takeovers are very unusual

7.3.7 Minority protection

Accoding to La Porta et al (1998; cited by Suáre and Santana-Martín 2004) a low level of protection of external investors' interest can be observed in Spain.

7.3.8 Composition of the board

Spanish companies have a one- tier board structure (Dalton, Daily, Johnson and Ellstrand 1998; cited by Suáre and Santana-Martín 2004).

The board consist of three types of directors. The first type contains internal directors, the so-called insiders of the firms. The second type contains external directors, who are not employed by the firm. Finally, the third type contains external directors who are not managers but have some personal and/or professional links with existing management. Because of these links with management these directors cannot be considered independent although externals. (Dalton et al 1998; cited by Suáre and Santana-Martín 2004).

7.3.9 Independence

According to Suáre and Santana-Martín (2004) the proportion of external directors on the board is around 50 per cent. No information about the proportion on independent directors is found.

7.3.10 The summary of the Spanish institutional system

- Family firms that exist in Spain apply a shareholder view.
- Spain has a high level of owner- concentration.
- Large shareholders in Spain are banks, companies and families.
- In most companies the CEO is a family member.
- Family members mostly control firms and the presence of non- family shareholders is insignificant.
- The majority shareholders are family groups and non- financial companies.
- The protective measures of ownership and control are; different voting power (rarely used), pyramid structures and cross- ownership.
- Proxies exist
- Performance based pay generally do not exist.
- Take-overs are unusual
- The protection of external investors is low.
- Spanish companies use a one- tier boar structure.
- Board structure consists of three types of directors:
    - Internal directors - employed by the company
    - External directors – not employed by company
    - External directors – non employed but with links to the company
- External directors form part of half of the board.

7.4 The Swedish institutional system

7.4.1 Ownership structure

According to Agnblad, Berglöf Högfeldt and Svancar (2001) the Swedish control structure is very concentrated and their research shows that the largest shareholder on average controlled 38 % of the voting rights of Swedish companies. In 34 % of the companies the controlling owner had more than 50 % of the votes and 82 % of the firms had a well- defined owner with more than 25 % of the votes. Therefore, a typical Swedish firm has one clearly defined controlling owner and in most cases the controlling owner is a family or a single individual (62 % or all listed companies). The same authors (Agnblad et al 2001) came to the conclusion that a large proportion of listed firms are privately controlled, mostly by family as a result of the use of dual- class shares. Therefore a controlling private owner can be a controlling minority shareholder that contributes with less than half of the capital but controls a majority of the votes.

According to Thim and Åkerberg (2003)[6] the largest owners of Swedish companies are institutional owners.

Large banks as in most continental European countries have played a main role, serving as house banks for major Swedish corporations. The 1934 Bank law forced banks to sell their shares, but the banks solved this by creating holding companies, which took over their portfolios of the banks and then distributed the shares to the shareholders of the banks. (Agnblad et al 2001).

Faccio and Lang (2002; cited by Thim and Åkerberg 2003) made a research of 245 companies between the years 1996- 2000 that shows that Sweden has a high dispersed ownership compared with other continental counties, such as Germany and Spain.

7.4.2 Pyramidal structures, cross- holdings and dual- class shares

Dual- class shares separate the votes from the equities and are a way of maintaining or establish control. The dual- class system (in Sweden) divides the shares between A and B shares, where the A share has a better voting right. (Agnblad et al 2001).

The voting right differential most common in Sweden is one to ten. In 1998 about 95% of all firms with dual- class shares used the one to ten differential. (Agnblad et al; cited by Henrekson and Jakobsson 2003).

Pyramid holding companies combined with dual- class shares are devices for private families to keep the control of the very large firms. Pyramid- holding companies have the corporate control of the largest firms on the Stockholm exchange. For example, Investor is a pyramid company with only two layers that primarily uses dual- class structures to separate control from ownership in the largest firms on the Stockholm Stock Exchange. (Agnblad et al 2001).

Sweden is one of the few countries that allows both pyramidal ownership structures and dual- class systems (La Porta et al1999; cited by Agnblad et al 2001). The use of different voting

[6] With the reservation of lack of empirical grounds

rights is common among a large proportion of the Swedish companies (Faccio and Lang 2000; cited by Thim and Åkerberg 2003).
These systems provide discretion to controlling owners that could lead to minority abuse but Agnblad et al (2001) states that it is hard to find violation of minority rights in Swedish companies.

The mechanisms used to establish separation of ownership and control are dual- class structures, pyramids and cross-holdings (Agnblad et al 2001).

New institutional owners from example the United Kingdom with a corporate governance system which are composed of formal rules and sanctions might find it hard to accept the widespread use of dual- class shares to separate votes from capital contributions. Even if listed firms are privately controlled and use dual- class shares international investors have a considerable and increasing presence. (Agnblad et al 2001).

7.4.3 Proxies

Proxy votes exist and can be given to another person, bank or a shareholder- organisation (Baums 1998; cited by Thim and Åkerberg 2003).

7.4.4 Performance based pay

The use of performance- related compensation in Germanic countries (such as Sweden) are rather limited. But variable compensation is becoming more and more important in these countries (Abowd and Bognanno 1995; cited by Weimer and Pape 1999).

7.4.5 Take-overs

Take-over bids in Sweden are normally negotiated between the main controlling owners of the bidder and the target- company and bids are almost universally non- partial and contingent upon 90 % of the shareholders accepting the offer. Compared with countries with dispersed ownership structures take-overs in Sweden are less and are often not possible without the consent of controlling parties. Hostile take-overs occur but are rare in Sweden. (Ericsson, Högfeldt and Spens 1998; cited by Agnblad et al 2001).

Thim and Åkerberg (2003) made the conclusion that market for corporate control in Sweden exists due to the fact that during 1996, there were 152 take-overs.

7.4.6 Minority Protection

Compared with United Kingdom, Sweden has a lower minority shareholders protection. However, compared with continental European standards (for example in Germany and Spain) Sweden has an average standard of minority shareholder protection. (La Porta et al, 1997, 1998 and 1999; cited by Agnblad et al).

But even if Sweden has a poor protection for minority shareholders, particularly for individual investors, the financial market is well developed with high level of market capitalisation. There is a relatively high amount of individuals that invests in shares primarily through funds and relatively high amount of firms goes public.

Sweden has a strong corporate law that protects minority shareholders. Sweden is also a trustful culture where outsiders feel protected from insider fraud but public securities markets are poorly developed according to Roe (2002).

7.4.7 Composition of the board

Sweden has a one- tier board structure (Wiemer and Pape1999).

7.4.8 The summary of the Swedish institutional system

- A typical Swedish firm has one clear defined owner. The Swedish control structure is very concentrated.
- Families privately control a large proportion of the listed firm.
- To separate ownership and control dual class shares, pyramids and cross- holdings are used.
- New institutional investors might not accept the use of the widespread use of dual-class shares.
- Proxy votes exist.
- Performance based pay hardly exist.
- Take-overs are unusual.
- The minority protection in Sweden is poor according to the two researches we have looked at. But importance of social prestige makes it a minor problem.
- A market exist for corporate control
- Compared with Anglo- Saxon countries, Sweden has a low minority protection.
- Swedish firms have a one-tier board structure

7.5 The comparison between the institutional systems

Through analysing the institutional systems existing in each county (United Kingdom, Germany, Spain and Sweden) we can now draw conclusions about which are the main characteristics of each system. These main characteristics are shown in the table below.

Countries Factors	United Kingdom	Germany	Spain	Sweden
Interest	Shareholders	Stakeholders	Shareholders	?
Ownership concentration	Dispersed	Concentrated Banks & other companies	Concentrated Families	Concentrated Family and bank
Pyramidal structures, Cross holdings and Dual- class shares	One-share- one-vote	One-share- one-vote	One- share- one-vote Cross- holding, Pyramid	Dual-class shares, Cross-holdings and Pyramid
Proxies	Used by managers	Used by banks	Used by shareholders	Used by all
Performance-based pay	Exist	Hardly exist	Hardly exist	Hardly exist
Take-overs	Common	Unusual	Non- existent	Unusual
Minority protection	Strong	Weak	Weak	Quite strong
Board structure	One- tier	Two- tier	One- tier	One- tier
Independence	Important	Not important	Externals not important	?
Stakeholders representatives	Not important	Important	Not important	Law- regulated

Table 8:1 ***Comparison of institutional systems***

The conclusions we have made of our institutional analysis is that United Kingdom and Spain has a shareholder economy where directors and managers are working towards shareholders' interest while Germany has a stakeholder economy where directors and managers are working towards stakeholders' interest. We have not found in which interest the directors and managers in Sweden are working.

Furthermore; Germany, Sweden and Spain have a concentrated ownership structure of their companies (large and controlling owners). In contrast United Kingdom has a dispersed ownership structure of their companies (many small shareholders without the ability to control the companies).

In United Kingdom, take-overs are a way of protecting shareholders from poor performance of managers and directors. Another way to protect the shareholders in United Kingdom is to tie some of the managers' and directors' compensation to business performance and to the creation of shareholder value.

In the other countries (Germany, Spain and Sweden) take-overs are unusual or non- existent and performance- based remuneration hardly exist.

Companies in United Kingdom, Germany and Spain use the principle of one- share- one vote, where in Sweden it is common for the owners to use dual- class shares to keep control of the companies. Sweden is also characterised by having pyramidal- structures and cross - holdings of their firms to further protect the control of the owners.

Proxies are used in every country but are most important in Germany where the banks use them to keep their voting- power and the control over the companies.

Take-overs are common in United Kingdom due to the dispersed ownership while the takeover market is quite weak in the other countries and therefore takeovers in these countries are unusual or non- existing.

The minority protection is strongest in United Kingdom in comparison with Germany, and Spain where such protection is weak. In Sweden minority protection is stated to be quite strong.

The board stucture in Germany differs from the other countries, since Germany has a two- tier board structure and the other countries have a one- tier board structure.

The independence criteria of the board is very important in United Kingdom, while in Germany it is not important and in Spain half of the board often are characterised by externals (owners or independent directors). In Sweden we have not found any information about independence.

The stakeholders' representatives on the board are important in Germany but not in United Kingdom and Spain. In Sweden the representation of employees is law- regulated.

Now we have made our final conclusions about the most important features of each of the institutional systems. Our next step to reach our aim – to find out if it is possible to unite the corporate governance codes existing in each country into one common code – is to see if the differences in the codes can be explained by the main features of each institutional system.

Therefore the next chapter will contain the total analysis.

8. Total analysis

In this chapter we will analyse if the differences found in the codes depends on the special features of the institutional systems found in the institutional analysis. The aim of this analysis, called the total analysis, is to conclude which recommendations of the code that will be hard to unite and which recommendations that will be possible to unite.

8.1 Duty of loyalty, duty of diligence and the conflict of interest

8.1.1 The Formal analysis

The recommendations of in which interest directors are supposed to work are differently stated in the codes since the British code recommends them to work in the best interest of the shareholders, the German and Spanish codes recommend them to work in the interest of the company while the Swedish code recommends them to work in the interest of both the company and the owners.

8.1.2 The institutional analysis and the conclusion

In the British institutional system, we can find a direct correspondence to the recommendation in the British code since we in our institutional analysis found that British managers and directors work in the best interest of the shareholders.

Since the German institutional system is characterised as a stakeholder system where directors are supposed to work exclusively in the best interest of the company, the system correspond to the German code.

The Spanish system is characterised by a shareholders' view, yet the code recommends the directors to work in the view of stakeholders.

We have not found this part in the Swedish institutional system; therefore we cannot compare the recommendations in the code with the institutional system.

The German and the British codes recommend directors and managers to work in different interest and these differences can also be found in the institutional systems. Therefore we conclude that these recommendations will be difficult to unite in one common code.

8.2 Composition of the board

8.2.1 The formal analysis

The German code recommends a two tier- board structure while the other codes recommend a one- tier board structure.
The British code recommends one half of the board to independent directors (both to company, managers and large owners) while the German code is missing this recommendation. Further the Spanish code recommends the majority of the board to be

externals (owner representatives or independent directors) and finally the Swedish code recommends the majority to be independent (to company and managers). The Swedish code also recommends two directors of the board to be independent to major owners and that there should be an equal proportion of men and women composing the board.

8.2.2 The Institutional analysis and the conclusion

The companies in United Kingdom, Spain and Sweden are characterized by having a one- tier board structure while the German companies have a two- tier board structure. Therefore the recommendations of the codes correspond to the institutional systems.

In the British institutional system the independent directors are judged as important members of the board. The recommendation of independent directors in the British code is therefore based on the institutional system.

The German system is characterised by the importance of stakeholders to form part of the supervisory boards instead of independent directors. In German companies, directors are appointed because of their banking, business or other relationship with the company. Employee representatives are also a characteristic of German boards, where half of the directors of supervisory board are employee representatives. Since the German code is missing recommendations about independence and contains the exact recommendations about employee representatives forming part of the board we can conclude that the recommendations in the German code is based on the German institutional system.

The Spanish institutional system shows that half of the directors are external directors (owners or independent directors) in Spanish companies. We can find the exact correspondence in the Spanish code.

We have not found features of the Swedish code especially emphasising independence of boards to be important; therefore we cannot make a conclusion.
We cannot find that the gender recommendation in the code is based on the Swedish institutional system. Rather we believe it has been set up because discussions about such issues.

In United Kingdom independent directors are important members of the board, therefore stated in the British code while in Germany it is more important with stakeholders as directors, therefore pointed out in the German code. We conclude that it will be difficult to unite these recommendations in one common code since the differences can be explained by the institutional systems.

8.3 Independence criteria of the board

8.3.1 The Formal analysis

The British code states that to maintain the independence an independent director cannot receive performance-based pay. This recommendation is missing in the other codes.

The independence criterion for inter-locking directorship is also differently stated in the codes. The British code states that a director is not independent if he/she is forming part of another board at the same time. The Spanish code states that a director is not independent if he/she forms part of another board of a company that is an owner of the first company and has a representative forming part of the board of the first company. The Swedish code states that; to be independent a director cannot form part of management of another company if that company has directors forming part of management in the first company.

The German code is missing a criterion for independence since it is missing a recommendation for independent directors to form part of the board.

8.3.2 The institutional analysis and the conclusion

The remuneration criterion in the British code is a consequence of the British institutional system since in United Kingdom remuneration is a way of aligning managers' and directors' interest with the interest of the shareholders. Therefore it is commonplace that both managers and directors receive performance- based pay. The recommendation in the British code stating that performance- based pay affects the independence of directors depends on that such remuneration may affect the independent directors' work. If receiving such remuneration the independent director might work in the best interest of the shareholders in a short- term basis rather in a long- term basis to receive as high wage as possible.
We cannot find that the criterion for inter- locking directorship in the British code is depending on the institutional system. Instead we think that this recommendation is to prevent companies from affecting each other.

The recommendation about the independence criterion stating inter-locking directorship in the Spanish code might depend on that it is usual for non- financial firms to have cross- holdings and pyramidal structures.

The Swedish code emphasises the importance of that managers not form part of a board in another company if that company has managers forming part of the board of the first company. We cannot find such counterpart in the Swedish institutional system. According to the code it is fully possible for an independent director to form part of several boards, even in boards' belonging to owners of the company. This probably depends on the high cross-holdings and pyramidal structures characterising the Swedish institutional system and the wish to protect the control of major owners.

We conclude that the differences in the recommendations about interlocking- directorship and remuneration are based on the institutional systems. Therefore we judge it difficult to unite these recommendations in one common code.

8.4 Term- limits

8.4.1 The formal analysis

The British and Swedish codes contain a recommendation about re-elections of directors. Such re- elections are a way of renewing the board[7]. The Swedish code also states that if a board is not renewed an explanation has to be made by the nomination committee.
The British code have special rules for the non- executives, stating, that their performance should be reviewed after six year on the board and if a non- executive is forming part of the

[7] Intervju (2004)

board for more than nine years he/she becomes subject to annual re- elections. The German and Spanish codes do not contain such recommendations.

8.4.2 The institutional analysis and the conclusion

In United Kingdom non- executives are supposed to work in the shareholders' interest. The recommendations in the British code about the re- election of non- executive directors indicate the importance that a non- executive director works towards shareholders' interest.

The reason why the German code does not recommend re- elections of directors might depend on that stakeholders form a significant part of the board and that directors are elected due to their knowledge and relations to the company and not by their independence.

The reason why the Spanish code does not recommend re- elections might depend on the concentrated ownership characterizing the Spanish institutional system and that managers and directors of the companies often own large stakes of the company.

We cannot find that the recommendation of term- limits in the Swedish code is based on the Swedish institutional system. We rather believe that this recommendation is stated to influence the companies to renew their boards.

We conclude that the recommendations about time- limits are difficult to unite in one common code since there are differences between the codes, which also can be explained by the institutional systems.

8.5 Chief executive officer CEO/Chairman

8.5.1 The formal analysis

The British and Swedish codes recommend a separation of the CEO and the Chairman. The German code separates the chairmen of management board and supervisory board. The Spanish code does not recommend such separation.

8.5.2 The institutional analysis and the conclusion

The reason why the Spanish code does not separate them might be that CEO's of Spanish companies often are large owners. Therefore, there is no need to supervise the work of the CEO since he/she probably works in his/her own interest and therefore also in other shareholders' interest.

Our conclusion is that an explanation for not dividing the CEO and chairman cannot be found in the Spanish institutional system. Therefore we believe that such a recommendation can be possible to unite. According to Expansión (expansión; 1 october 2003), 30% of the Spanish companies in the year 2003, had separated CEO and chairman. This shows that such separation is possible, although it might be costly for the companies.

8.6 Proposed committees

8.6.1 The formal analysis

The British, Spanish and Swedish codes recommend companies to form nomination committee, remuneration committee and audit committee. The German code only recommends companies to form an audit committee.

8.6.2 The institutional analysis and the conclusion

We cannot find any reason in the German institutional system that would make it impossible for German companies to form nomination or remuneration committees. The reason why the German code has not recommended these committees probably depends on that the supervisory board is carrying out the tasks of such committees.

The conclusion is that this part can be united in a common code since we cannot find any institutional features that can explain the differences in the codes.

8.7 Nomination committee

8.7.1 The formal analysis

In the formal analysis the recommendations of the composition of the nomination committee were concluded difficult to unite since the British code recommends that the majority of members of the nomination committee should be independent while the Spanish code recommends that all members should be externals (owners or independent directors). Further the Swedish code recommends the majority not to be directors and that senior managers should not form part. Finally the German code does not have a recommendation about a nomination committee

8.7.2 The institutional analysis and the conclusion

We conclude that the composition of the nomination committee depends on the different owner- structures in the institutional systems.

The British code might recommend that the majority of the nomination committee should be independent because of the importance of independent directors to work for the shareholders' interest.

The Spanish code might recommend the majority to be externals because they represent the interest of both major owners and minority owners.

The Swedish code might recommend half of the members to be non- directors because the directors should not nominate themselves. We cannot find that the recommendations in the Swedish code about the composition of the nomination committee depend on the institutional system.

The recommendations about the nomination committee can be difficult to unite in one common code since there are needs to protect the interest of shareholders in the institutional systems, depending on the different ownership structures characterising the systems.

8.8 Remuneration committee

8.8.1 The formal analysis

The recommendations for composition of remuneration committee are differently stated in the codes.
The British code recommends at least three members to be independent while the Spanish code recommends all to be external directors (owners or independent directors). Further the Swedish code recommends all members to be independent to senior management and company but not to owners. Finally the German code is missing a recommendation about remuneration committee.

8.8.2 The institutional analysis and the conclusion

In the British code the recommendation about composition is influenced by the dispersed ownership and the importance of independent directors to form part. In the institutional analysis we found that it is especially important that independent directors participate in the decisions of the performance-based remuneration for executives, which should align the interest of executive directors with the interest of minority shareholders.

In the Spanish and Swedish codes the recommendations about the composition of the committee probably are influenced by the concentrated ownership in the institutional systems. Because of strong owners of the companies in such systems, it is more important for the owners themselves to decide the remuneration existing in their companies.

The differences in the recommendations about the composition of the remuneration committee in the codes are based on the institutional systems and the importance of independent members to form part. The conclusion is therefore that these recommendations can be difficult to unite in one common code.

8.9 Audit committee

8.9.1 The formal analysis

The recommendation of the audit committee that is most notable is the recommendation about the composition. The British code recommends at least three directors, which all should be independent, while the German code recommends that no former member of management board or present member of supervisory board should form part. The Spanish code recommends that all should be externals. The Swedish code recommends that managers should not form part and that the majority should be independent to company and senior management and one member should be independent to major shareholders.

8.9.2 The institutional analysis and the conclusion

The recommendations in the codes stating the composition of the audit committee might be explained as in the nomination and remuneration committee; by concentrated or dispersed ownership structures. The only difference is that the Swedish code for this committee recommends that one member should be independent to major shareholders. This recommendation probably depends on that strong owners have control over Swedish firms and that they also have to be reviewed.

The conclusion is that this part is difficult to unite in one common code even though the work of the committee is quite similar in the codes the composition once again differs between the codes. The recommendations about composition are based on the institutional systems and the different importance of independent members to form part. The conclusion is therefore that these recommendations cannot be united in one common code.

8.10 Remuneration

8.10.1 The formal analysis

The British code recommends remuneration to be divided between executive directors, non-executive directors and non-executive independent directors. The code recommends incentive pay to be aligned with shareholders' value. The German code divides the remuneration between the management board and the supervisory board. The Spanish code let the company it self decide but the remuneration has to be disclosed and transparent. The Swedish code separates the remuneration of senior management and directors.

8.10.2 The institutional analysis and the conclusion

It is important in the British institutional system to align the directors' and managers' work with shareholder value, therefore also stated in the code.
We cannot find similarities between the recommendations made in the German, Spanish and Swedish codes and their institutional systems.

Therefore we conclude that the recommendations about remuneration can be united in one common code because we have not found any barriers for this in the institutional systems

8.11 Shareholders' meeting

8.11.1 The formal analysis

The most important difference is that the British and Spanish codes emphasize the importance of institutional investors' participation at shareholders' meeting. The British code also emphasizes the importance of keeping contact with major shareholders. The Swedish code recommends directors, chairmen of committees, CEO and the auditor to participate at the shareholders' meeting.
The recommendation of proxies is stated in the British, German and Spanish codes. The one-share- one- vote principle is only stated in the German code.

8.11.2 The institutional analysis and the conclusion

Here we can find many connections between the codes and the institutional systems.

Firstly the importance of institutional shareholders participation in the British code can be explained by that these investors are large shareholders with the opportunity to monitor

British companies but that at the moment are not using their votes. The importance of keeping contact with major shareholders is probably emphasizes for the same reason.

The reason why the Swedish code recommends so many directors, managers and auditors to participate at shareholders' meeting probably depends on the concentrated ownership. On the shareholders meeting the owners can monitor the companies by using their voting power through dual- class shares. Shareholders' meeting is of importance for shareholders to affect the company and therefore it is important for many members of the organization to participate to give the sufficient information to make a decision.
The reason for the Swedish code not to recommend proxies to be used is not based on the Swedish institutional system since they also can be used to vote at shareholders' meeting in Sweden.

The one- share one vote principle is only stated in the German code and can be found in the German institutional system. The one-share, one- vote principle is not recommended in the code but can be found in the British and Spanish institutional system as well. In the Swedish institutional system dual- class shares are very important for the owners to keep their control since they often owns less than the majority of capital and are commonly used.

The institutional shareholders are important in the British institutional system therefore stated in the code. These investors are not important in the Spanish institutional system, yet stated in the code. The institutional investors may also become more important in other countries of Europe due to the new pension funds becoming new external providers of capital. Therefore we conclude it possible for the German and Swedish code also to set up guidelines for such investors.

The recommendation in the Swedish code about participation at shareholders' meeting can be united in one common code since there are no institutional factors making such recommendations impossible in the other codes.

Proxies are not either difficult to unite in one common code because of the institutional system in Sweden also states that they could be used.

The recommendation of the one- share- one- vote principle is impossible to unite since dual-class shares are very important in the Swedish institutional system for owners to keep the control over the companies. Therefore the unification of the recommendation of the shareholders meeting is impossible due to the different owner-structures in the institutional systems.

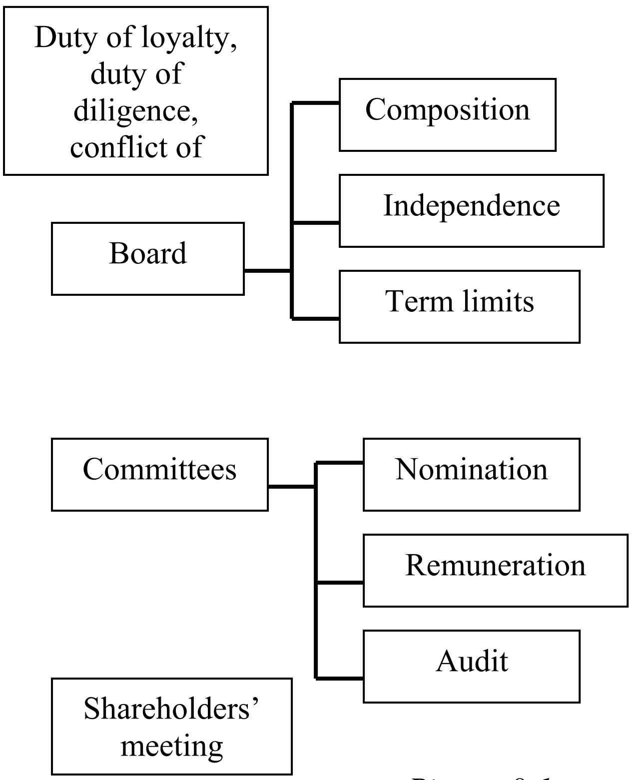
8.12 The possibilities for a common code

In the formal analysis we started by comparing the British, German, Spanish and Swedish codes of corporate governance to conclude if it was possible to unite all recommendations stated in each code. To be able to compare the recommendations stated in each code we created an analysis model. In the conclusion of the formal analysis we concluded that some parts could be united and that some parts were more difficult. In the following analysis, the institutional analysis we searched for special features existing in the British, German, Spanish and Swedish institutional systems. These features were then used in our total analysis to find out if the differences in the codes where depending on the institutional systems.
If the differences in the recommendations were depending on the institutional systems, we concluded the recommendations difficult to unite, since the institutional systems are difficult to change. If the differences were not depending on the institutional systems, then, we concluded them easier to unite.

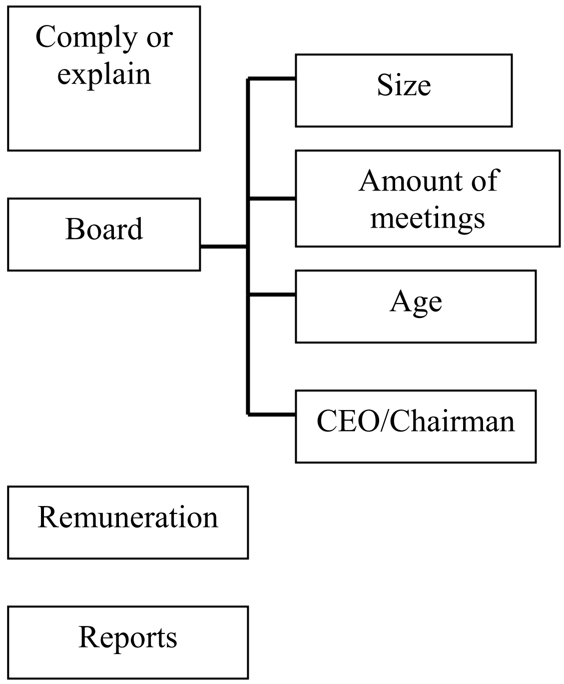
The recommendations that we have concluded to be difficult to unite are the ones treating; duty of loyalty/duty of diligence and conflict of interest, composition of the board, independence on the board, term limits for directors, the nomination committee, the remuneration committee, the audit committee and the shareholders' meeting (*picture 8:1*).

The recommendations that we have concluded possible to unite are the ones treating; the comply or explain principle, the size of the board the amount of meetings the board should hold, the age of directors, CEO/chairman, the remuneration and the reports (*picture 8:2*).

Not possible to unite | **Possible to unite**



Picture 8:1



Picture 8:2

9. Conclusion

In this chapter we will state our conclusion of the research and suggest further research in the area of corporate governance codes.

The aim of our research was to come to the conclusion if it is possible to unite corporate governance codes in Europe into one common code of the European member states.

To reach our aim, firstly, we looked into four different codes today existing in Europe, the British Combined code, the German Cromme code, The Spanish Ley Aldama and the Swedish code for corporate governance. In our first analysis we used our analysis model to compare the codes and we came to the conclusion that the recommendations where of such difference that a common code containing all the recommendations would not be possible to implement. But we also found recommendations that were possible to unite, since differences in the codes not were of significance.

In our second analysis we analysed the different institutional systems existing in United Kingdom, Germany, Spain and Sweden. The purpose of that analysis was to find out if the characteristics of each institutional system could explain the differences in the codes.

In our third analysis we finally compared the corporate governance codes with the institutional systems to find if the significant differences in the codes could be explained by the systems. If the recommendations could be explained by the institutional systems we concluded that it would be hard to unite the recommendations in one common code since institutional systems are hard to change. In this analysis we came to the conclusion that many of the recommendations in the codes are depending on the institutional systems and will therefore be difficult to unite.

We were surprised to come to this conclusion since we did not believe that the European countries had such different structures of their firms, their ownership structure of the companies, their financial markets and their belief how companies should work and in which interest they should work for.

The year 2002 a group called; the high level group of company law expert where given the task by the European commission to come to the conclusion if it could be possible to implement a common code for all the European member states. The work- group came to the conclusion that a common code is not possible to implement based on the fact that company laws are in certain aspects widely divergent between the European countries and to achieve a common corporate governance code while leaving company law untouched would not be feasible.

The aim with our research was to find out if the institutional systems where influencing the differences between the codes rather than the laws of the countries. And we came to the conclusion that there were many recommendations in the codes based on the different institutional systems. Our analysis of the institutional systems is weak and through further analysis we could probably find out which exact feature of the financial systems is the most important, influencing the other features.

So our conclusion is that the problem for the multinational listed company with its core business in Germany and other business in United Kingdom, Spain and Sweden still withstands since this firm probably will follow one corporate governance code to create shareholder trust but could at the same time even loose trust in the other financial markets.

Each year the European commission draft different recommendations for the European member- states to set up in the codes. This is a way of converge the codes into one eventually. The future is to decide.

9.1 Further research

In our research we have only compared four countries in the European union. It could be possible to make further research of other county- codes as well. An interesting area could be to analyse the possibilities to implement a common code in the Scandinavian countries, where the goal is to create a common stock- market. It could also be interesting to further look into the corporate governance codes in the Eastern European countries.
The Swedish code will be implemented during 2005 so it would be interesting to analyse how the Swedish will follow the code and how they will show it to the financial market. The implementing of the Swedish corporate governance code also means more work for all company- organs, but what will it exactly mean for the auditor? Will the auditor have more work and in which areas?

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Codes

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