

**Tables 1 and 2: Post-War Corporate Governance Models in the United States and Germany (c. 1985)**

<b>United States</b>		
<b>Regulation</b>		<b>Correlated Practice</b>
<b>Securities Law</b>	Centralized federal securities regulation in rulemaking & enforcement by SEC; Stringent and highly prescriptive transparency & disclosure rules; Self-regulation of accounting industry & Financial Accounting Standards Board (FASB)	Securities markets highly capitalized, substantial use of equity finance and financial innovation; Fragmentation of ownership (separation of ownership & control); Weak oversight of accounting industry relies on professionalism and reputational capital
<b>Company Law</b>	State law governs internal firm structure & affairs (no uniform federal corporate law); Hierarchy of fiduciary duties favors shareholder supremacy over other stakeholders; Corporate law statutes and jurisprudence permits wide variety of anti-takeover defenses	Broad managerial and board discretion in running firm; Corporate law and intra-firm governance favors managerial interests; Stakeholders receive little legal protection, creating bias in favor of short-term financial interests; Fiduciary law weakened—strengthens position of managers and limits protection of shareholders & stakeholders alike;
<b>Labor Law</b>	Framework for voluntarist organization and firm-level bargaining; Sharply differentiated from corporate law	Weak, fragmented labor unions; Contractual labor relations separate from firm governance; No codetermination structures of employee representation
<b>Enforcement Mechanisms</b>	Formal & litigious enforcement of complex prescriptive rules; Reliance on private litigation for enforcement	High incidence of litigation and strike suits; Wealthy and politically active plaintiffs' bar

<b>Germany</b>		
<b>Regulation</b>		<b>Correlated Practice</b>
<b>Securities Law</b>	Weak state transparency regulation; No federal regulation or regulator	Opaque financial reporting; Bank-centered financial system & undeveloped securities markets; Concentrated ownership
<b>Company Law</b>	Federal company law imposes uniformity & prevents competition; Supervisory board	No hierarchy of legal interests in fiduciary law; Stakeholder system of representation & governance
<b>Labor Law</b>	Neo-corporatist sectoral bargaining framework; Works council codetermination	Cooperative labor relations rests on strong unions within firm and political system; Functional split between unions and works councils takes wage issues taken out of firm governance; Work hours, organization, etc. resolved through firm governance
<b>Enforcement Mechanisms</b>	Few mechanisms of formal legal enforcement; Procedural and substantive restrictions on private litigation	Governance by negotiation among opposing interests; Replication of neo-corporatist patterns within the firm

**Table 3: Major Changes in Financial Market Law and Regulation in the United States (1990-2002)**

<b>Reform</b>	<b>Rationale/Effect</b>
<ul style="list-style-type: none"> <li>• 1992 reform of SEC proxy rules allow shareholders to communicate about governance issues without filing proxy statements.</li> <li>• 1995 Private Securities Litigation Reform Act grants institutional shareholders “lead plaintiff” status in shareholder litigation and raises pleading requirements in fraud suits.</li> <li>• 1998 Securities Law Uniform Standards Act preempts state securities law and lawsuits to impose restrictions on securities litigation.</li> <li>• 2000 Regulation FD (Fair Disclosure) bans selective disclosure of material information to favored institutions and analysts.</li> <li>• 2002 Sarbanes-Oxley Act:             <ul style="list-style-type: none"> <li>➢ Requires certification of corporate financial statements by CEOs and CFOs, with sanctions for material inaccuracy.</li> <li>➢ Expands SEC authority over accounting industry rules &amp; practices.</li> <li>➢ Creates Public Company Accounting Oversight Board to draft accounting regulations.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Institutional investors given more power and influence by reducing restrictions on and costs of greater cooperation in governance activism.</li> <li>• Power reallocated to institutional investors in effort to curb securities litigation; alters structure of status and legal authority among shareholders.</li> <li>• Preserved “tort-reform” from circumvention under state law; unprecedented centralization of securities law at federal level.</li> <li>• Requires uniform public disclosure to “level the playing field”, but conflicts with the goals of institutional activism and 1992 proxy reforms.</li> <li>• Improved transparency and governance:             <ul style="list-style-type: none"> <li>➢ Increased incentives for accuracy in disclosure by increasing potential sanctions against managers.</li> <li>➢ Increases stringency of accounting rules and principles and declares self-regulation a failure.</li> <li>➢ Creates structure under SEC control to develop accounting rules and regulate accounting profession.</li> </ul> </li> </ul>

**Table 4: Major Changes in Company Law in the United States (1990-2000)**

<b>Reform</b>	<b>Rationale/Effect</b>
<ul style="list-style-type: none"> <li>• State judicial rulings in takeover litigation in the 1980s and early-1990s sanction the adoption of anti-takeover defenses and prohibit others.</li> <li>• State anti-takeover statutes impose restrictions on mergers and allow consideration of non-shareholder interests by the board in responding to takeover threats.</li> <li>• 1999 NYSE and SEC rule amendments exempt most stock option plans from shareholder approval.</li> <li>• Sarbanes-Oxley Act of 2002 extends federal law into internal corporate structure for first time; requires:             <ul style="list-style-type: none"> <li>➤ Board must have a majority of “independent”<sup>*</sup> members;</li> <li>➤ Board must form auditing, nominating, and compensation committees comprised of independent directors;</li> <li>➤ Auditors hired by and report to board instead of management;</li> <li>➤ Board must create and oversee firm’s risk management policies.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Weakens shareholder rights &amp; market for control.             <ul style="list-style-type: none"> <li>➤ Prescriptive: prohibition of some defenses.</li> <li>➤ Structural: compliance with fiduciary duties mandates board and shareholder voting procedures re: anti-takeover defenses.</li> </ul> </li> <li>• Reallocates power to board and management; weakens shareholders.</li> <li>• Weakens shareholders in setting managerial compensation.</li> <li>• For first time in U.S. history, federal law intervenes in traditional areas of state corporate law.             <ul style="list-style-type: none"> <li>➤ Seeks to ameliorate agency problems/conflicts of interest between managers and shareholders.</li> <li>➤ Mandatory modification internal structure of corporation designed to protect shareholders where market regulation has proved inadequate.</li> <li>➤ Restructuring of board designed to improve and complement securities regulation disclosure rules.</li> <li>➤ Increases board’s oversight role and institutes self-regulation within firm.</li> </ul> </li> </ul>

---

<sup>\*</sup> SEC authorized under the Act to promulgate standards defining “independence.”

**Table 5: Major Changes in Financial Market Law and Regulation in Germany (1990-2000)**

<b>Reform</b>	<b>Rationale/Effect</b>
<ul style="list-style-type: none"> <li>• 1994 Second Financial Markets Promotion Law creates the first federal securities regulator (the BAWe) and disclosure regulation.</li> <li>• Securities Trading Law of 1995 requires disclosure of parties owning or controlling 5% of stock.</li> <li>• 1998 disclosure law allows firms to issue financial statements using either IAS or US GAAP.</li>   <li>• 1998 KonTraG proxy voting rules require internal bank procedures and offices to reduce conflicts of interest.</li> <li>• 2001 legislation consolidates regulatory authority over all financial services (securities, banking, and insurance) within one agency (BAFin)</li> </ul>	<ul style="list-style-type: none"> <li>• Increases disclosure and enforcement capacity in securities markets to encourage use and development of equity finance.</li> <li>• Increases transparency, protects small shareholders, but law has significant loopholes.</li> <li>• Intended to increase transparency through more stringent accounting rules (US GAAP and IAS more stringent than German accounting standards).</li>   <li>• Internal restructuring of bank proxy voting protects shareholders from conflicts of interest between shareholders and banks as lenders.</li> <li>• Increased efficiency of regulatory administration and recognition of blurring of financial services.</li> </ul>

**Table 6: Major Changes in Company Law in Germany (1990-2000)**

<b>Reform</b>	<b>Rationale/Effect</b>
<ul style="list-style-type: none"> <li>• Courts infer existence of fiduciary duties to shareholders (1980s-1990s), but law remains undeveloped and conceptions of corporate interest distinct from shareholder interest persist.</li> <li>• 1998 KonTraG statute:               <ul style="list-style-type: none"> <li>➢ External auditors hired by and report to board instead of management;</li> <li>➢ 1 share, 1 vote rule;</li> <li>➢ Stronger fiduciary obligations of custodian bank in voting proxies;</li> <li>➢ Limited voting of bank-controlled shares and proxies;</li> <li>➢ Prohibition on voting cross-shareholding stakes in board elections;</li> <li>➢ Stock repurchases allowed for first time.</li> </ul> </li> <li>• 2000 tax reform law designed to break up cross-shareholdings.</li>   <li>• 2001 Takeover Law:               <ul style="list-style-type: none"> <li>➢ Imposes mandatory bidding procedures.</li> <li>➢ Duty of neutrality in responding to takeover threats.</li> <li>➢ Permits stronger anti-takeover defenses.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Rulings seek to protect shareholders, but effect limited.</li>   <li>• Modernize company law to protect shareholders.               <ul style="list-style-type: none"> <li>➢ Enhances transparency and reallocates power from management to supervisory board.</li> <li>➢ Shareholder democracy protects minority shareholders.</li> <li>➢ Weakens bank power while retaining shareholder voting outside of management control.</li> <li>➢ Weakens managerial power through network “logrolling”.</li> <li>➢ Liberalizes restrictions on corporate finance and compensation practices.</li> </ul> </li>   <li>• Increases liquidity of securities markets by increasing proportion of traded shares; weakens managerial power through network “logrolling”.</li> <li>• First statutory regulation of takeovers:               <ul style="list-style-type: none"> <li>➢ Ensures fair treatment of minority shareholders</li> <li>➢ Strengthens and protects shareholder interests</li> <li>➢ Protects managerial and stakeholder interests against short-term shareholder interests.</li> </ul> </li> </ul>

**Tables 7 and 8: Modified Governance Models and the Effects of Reform (1990 vs 2002)**

<b>United States</b>		
	<b>1990</b>	<b>2002</b>
<b>Securities Law</b>	Proxy rules encumber shareholder activism by institutional investors Proxy rules (and state corporate law) give managers almost complete control over board nominations and elections; Accounting industry self-regulating; Accounting rules drafted by private industry body (FASB)	Liberalization of proxy rules to strengthen governance role and power of institutional investors; Amended proxy rules to (modestly) increase the ability of shareholders to nominate and elect directors; Strengthened transparency regulation through more stringent disclosure, risk management, and executive certification of corporate accounts; Federal regulatory control over accounting rules by the PCAOB under SEC supervision
<b>Company Law</b>	Corporate law and fiduciary duties under control of state lawmakers and judges; Corporate law generally extremely permissive regarding board structure, responsibilities, and legal duties	Sarbanes-Oxley Act partially displaces state corporate law by requiring greater board independence, director qualifications, board control over auditing, and expanded board powers to monitor management
<b>Labor Law</b>	Virtual exclusion of labor from firm management and governance	No change
<b>Enforcement Mechanisms</b>	Liberal substantive and procedural rules for private litigation; SEC has broad enforcement powers but resources fall below demand during 1990s; State authorities are minor presence in enforcement	Tort reform imposes stricter pleading requirements, encourages institutional investors to act as “lead plaintiffs”, and pre-empts state securities laws; Increased SEC enforcement of civil & criminal penalties; Dramatic increase in state-level enforcement actions and suits

<b>Germany</b>		
	<b>1985</b>	<b>2002</b>
<b>Securities Law</b>	Decentralized securities regulation and securities market oversight at the state (Land) level Weak disclosure and transparency rules	Complete overhaul of law and regulatory structure; Centralization of regulation in single federal regulatory agency; Creation and steady strengthening of transparency and disclosure rules
<b>Company Law</b>	Weak fiduciary duties and supervisory board under federal law; Unequal voting rights and share voting caps permitted; Voluntary takeover rules (no formal or enforceable law); Labor representation on supervisory board of listed firms	Supervisory board responsible for auditing and risk management; Institution of one share-one vote rule; Liberalization of takeover law with allowance of anti-takeover defenses; Supervisory board codetermination unchanged
<b>Labor Law</b>	Labor representation in firm governance through works council codetermination	Works council codetermination strengthened by making election easier & expanding information and consultation rights
<b>Enforcement Mechanisms</b>	Weak governmental investigatory and enforcement powers; Procedural and substantive law discourages private litigation	Federal securities regulatory given formal powers of investigation; Marginal strengthening of private litigation rules

