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THE MAIN MODELS OF CORPORATE GOVERNANCE

Abstract:

Corporate governance represents a set of processes and policies by which a company is managed, controlled and directed to achieve the predetermined management objectives settled by its shareholders. The development of corporate governance has been affected by a number of models that have been developed over the years. Thus, in our research, we are trying to determine the common elements, and also, the differences that have occured between the traditional model of corporate governance, german model, japonesse model, and also, islamic model. Taking into consideration that each country has its specific economy characteristics and also, individual culture, we intend to identify the best model that is suitable for each area.

Keywords:

traditional model of corporate governance, german model of corporate governance, japonesse model of corporate governance, islamic model of corporate governance, stakeholder, shareholder.

JEL Classification: G34

1. Introduction

The 21st century saw a massive growth in the development of corporate governance concept, whose time has come. After the world's most famous scandals, such as Enron, Parmalat, WorldCom, Maxwell or Lehman Brothers, the importance of corporate governance has been understood by both developed and developing countries. But, what represents more exactly corporate governance? As defined by the Organization for Economic Cooperation and Development (OECD, 2004), corporate governance represents the assembly of traditions, procedures, norms, rules and regulations, both formal and informal, by which an entity is managed and through which are established relationships between major parties interested in a company, who can be either its shareholders, managers or members of the Board of Directors, and all the organization's links with other interested parties such as creditors, suppliers, employees, governmental authorities or local community. In this sense, corporate governance is not just a simple relationship between the company and the holders of financial capital (its owners), but it involves the system of relations existing between the enterprise and all stakeholder groups interested in its development.

Reported to the specific economic, financial, political, social or cultural characteristics of each state, the corporate governance systems have certain characteristics and defining elements that distinguish them from one country to another. In the specialized literature, many authors have tried to determine the right classification of corporate governance systems, but their attempts to spot pattern categories for these systems (with features for each country), which have failed of course, were compared (Solomon, 2010) to Cinderella's stepsisters useless efforts to fit in her shoe. From our point of view, selecting a model of corporate governance to put it in practice in a specific country is quite difficult, as the corporate governance structure of each country evolves by reference to the factors and conditions within it. However, we believe that certain classifications are useful to researchers in the steps they take, especially for future developments of the chosen theme.

2. Definition and scope of corporate governance

According to Sir Adrian Cadbury report on financial aspects regarding corporate governance (Cadbury, 2000), corporate governance represents a set of processes and policies by which a company is administered, controlled and directed to achieve the predetermined management objectives settled by the shareholders. Moreover, according to this report, the aim of corporate governance is to maintain a balance between economic and social goals and also, between individual and communal goals.

However, it is important to mention that corporate governance is different by management: while the management runs the enterprise, the board of governing body ensures that the organization is being run well and also, in the right direction (Tricker, 2009).

The most important benefits of the corporate governance to the organisations are related to business success, investor confidence and minimisation of wastage. For business, the improved controls and decision-making will aid corporate success as well as growth in revenues and profits. For the investor confidence, corporate governance will mean that investors are more likely to trust that the company is being well run. This will not only make it easier and cheaper for the company to raise finance, but also has a positive effect on the share price. When we talk about the minimisation of wastage, we relate to the strong corporate governance that should help to minimise waste within the organisation, as well as the corruption, risks and mismanagement.

Although corporate governance plays an important role in the heart of a company, it may sometimes lead to some problems in a corporation, as a consequence of its complex structure. In this respect, it can be difficult to regulate who will control the employee, to know which is the limit of the risk of investment that can be beared by the company, how company will take into account welfare of shareholder and stakeholder and also, how the board will be elected and who will be a member in a board. These questions can be expended and almost every corporation can face these problems in financial markets. This variety in corporate governance may lead to some fundamental issues in the company

3. Models of corporate governance

As we have mentioned above, due to the cultural, historical and financial differences between countries, there are some different corporate governance systems in the financial markets. In what follows, we present the corporate governance systems applied in developed countries, namely: the traditional (Anglo-Saxon or Anglo-American) model, the German model, the Japanese model and finally, the Islamic model.

3.1 Traditional Anglo-Saxon Model

The traditional model is a shareholder type model, which means that the attention is focused on shareholders and is currently used for governing corporations in the United States, Great Britain, Australia, Canada, New Zealand, South Korea or Chine. According to this model, the corporation’s main objective is to maximize the value for investors, with focus on the outsiders or external shareholders. Regarding this issue, in the United States and Britain, is known the tendency to involve more outsiders and fewer insiders in the corporate governance structure, in order to avoid the abuse of power. For example, a Board of Directors held firmly by a person serving both as chairman and CEO or a Board of Directors composed solely of insiders are interested in keeping the power on for longer without taking into account the interests of other participants. However, these countries lately tend to exhibit substantially their management structure. Thus, outsiders become insiders as institutional shareholders get hold of the majority shares in a corporation and exert a strong influence on management, taking over the role of major insider.

The model is based on a well-developed regulatory framework which stipulates the rights and responsibilities, and relationships between the key players that make up the triangle of corporate governance, namely: managers, directors and shareholders.

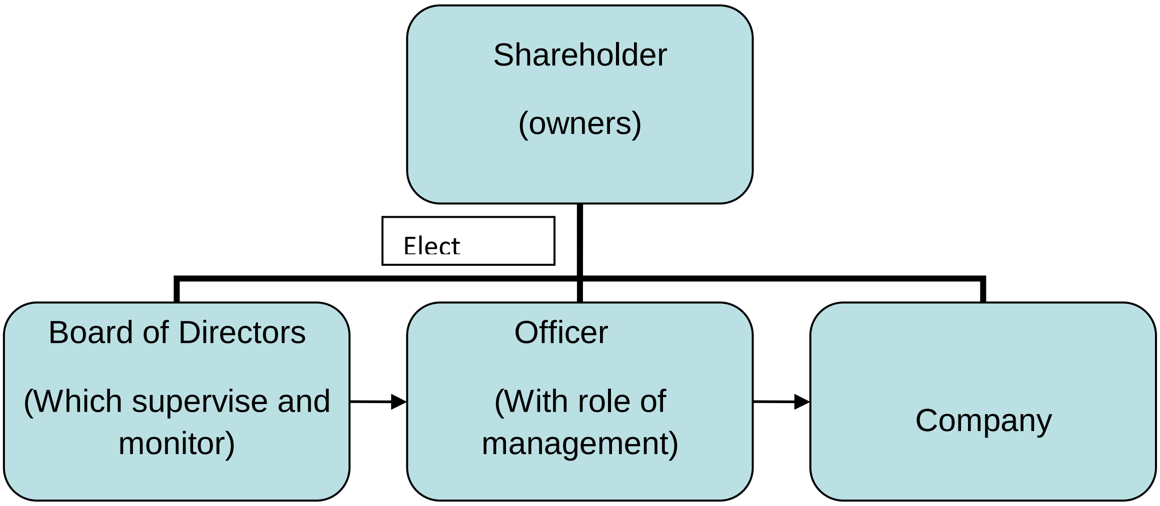
Since it is an outsider type model, the traditional model has the characteristic that investors contribute with capital in order to maintain the ownership right within the group but they generally avoid to assume legal responsibility for corporate activities. In this respect, on the one hand, they give up the managerial control in favor of leaders who are paid to act as their agents, and on the other hand, they continue to monitor them in order to ensure that whether external agent works for the benefit of the company (Coyle, 2005). The main features of this model relate to the separation of ownership and control: the costs of this separation of ownership and control are called agency costs. However in this case, the problem is that the interests of managers and shareholders do not always coincide. To reconcile these conflicts, a Board of Directors is elected by the shareholders with the role of overseeing the management process on their behalf and in their interest. This model consists of a single board of directors (one-tier) system (Salacuse, 2004). Therefore, the Board of Directors provides two functions: business management - achieved by insiders (executive management in which the supreme authority is the CEO) and supervision and control - performed by outsiders (acknowledged as non-executive directors in the British system).

Also, another feature of the traditional model is that stock exchanges play an important role in establishing the requirements for listing and information. The disclosure requirements are set at high standard, but nowhere are they as stringent and complex like in the United States. From the multitude of them, we point out the following: a breakdown of the capital structure, corporate financial data, detailed and substantial information on each candidate to the Board of Directors, information on mergers and restructuring, amendments proposed to the Articles of Association etc. The listing requirements from the UK and other countries using the Anglo-American are similar, with the specification that less data, but from a variety of categories, is required.

The corporate actions requiring shareholders' approval are divided in two categories: routine action and non-routine actions. Routine actions require the approval of shareholders and include the election of directors and the selection of auditors, and on the other hand, the non-routine actions, even if they require the approval of the directors, refer to mergers, takeovers and restructurings, as well as the amendment of Articles of Association.

However, there is a significant difference between the American and British system, namely: the USA shareholders do not have voting rights on the dividend proposed by the Board of Directors, while in Britain the shareholders have this right. Regarding the right to vote, the traditional model allows voting by proxy, without shareholders attending the General Assembly, the process taking place as follows: shareholders receive by e-mail the agenda of the meeting, including information on all drafts, annual c report of the corporation and a voting card, which must be completed and returned by e-mail to the corporation. Thus, the shareholders authorize the Chairman of the Board to consider votes as indicated on the card.

Figure no. 1 - Traditional Anglo-Saxon Model



Source: Own processing.

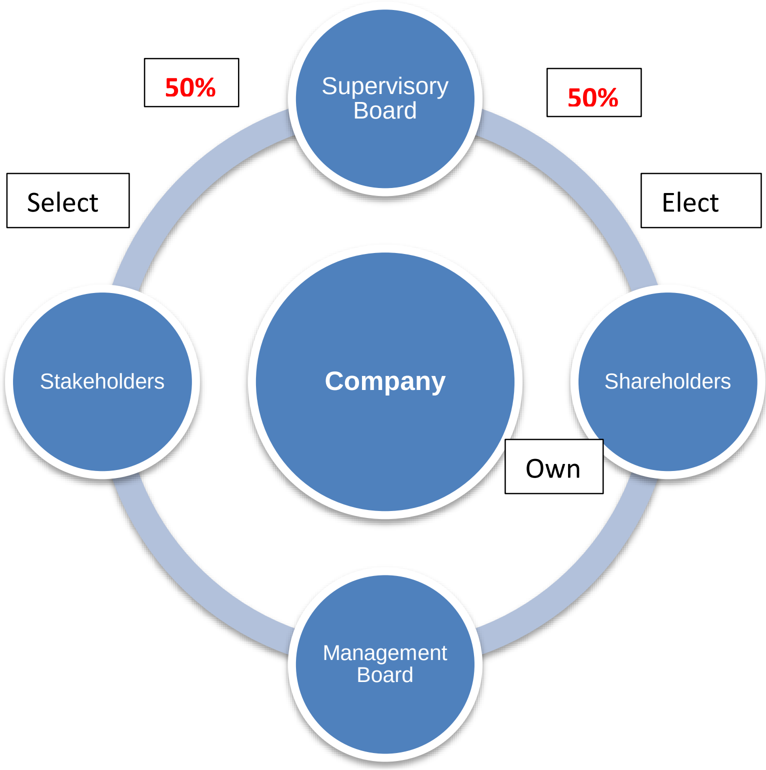
3.2 German Model of Corporate Governance

This model is also known as a Continental European approach, because it is implemented by many European states, such as Germany, Holland and France. The German model of corporate governance is a model more original compared to the other ones, its originality being conferred by the existence of a number of influential shareholders, like credit institutions. Within this model, the focus is no longer on the capital markets and stock exchanges, but on insiders, i.e. the shareholders involved in the management and control of corporations.

Credit institutions are participating actively in the recovery of distressed companies by increasing their equity capital. The management of these portfolios should be done taking into account the banks' responsibility towards their clients in order to ensure the safety of savings. Collaboration between credit institutions and corporations has the effect of reducing the information asymmetry in order to facilitate the access to bank capital.

Therefore, in the case of German corporate governance model we're not dealing with a "one-tier" (on one level) corporate structure like in the Anglo-American model, but with a "two-tier" (on two levels) structure, in which the Board of Directors is responsible for the management and business administration of corporate activity and the Supervisory Board has the role of supervising the management, selection, appointment and dismissal of leaders, endorsement of Board members, contracting auditing services (Fernando, 2006), as it is highlighted in the Figure no. 2.

Figure no. 2 – German Model



Source: Interpretation after the following book: Fernando, 2006, p. 54.

Also, another fundamental characteristic of the German model of corporate governance lies in the principle of social co-determination, namely the presence of employees' representatives on the Supervisory Board, which gives them control over management and the right to take part in the decision-making.

Therefore, we can clearly observe in this model the central role assigned to human resources and intense preoccupation to satisfy the interests of employees, taking into account their opinion. At the same time, it is obvious the German model is a model of social consensus, which encourages a mechanism of co-management, i.e. a participatory management, and a process of decision making with a strong democratic feature, which helps increasing productivity and reducing various risks that affect corporations.

3.3 Japanese Model of Corporate Governance

The Japanese model is characterized by the fact that credit institutions and other companies hold shares in corporations. Similar to the German model, credit institutions have a strong connection with corporations within the Japanese model.

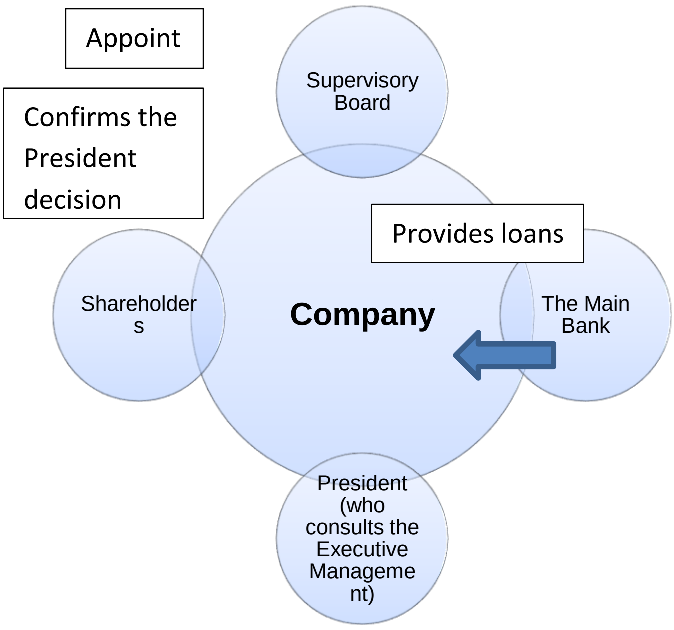
The Japanese economy is dominated by the so-called *keiretsu*, representing major companies grouped around a credit lending institution that are collaborating in order to achieve a mutual benefit. In most cases, a company holds shares of other companies that are members of the group, thus having an influence on the decision-making process.

Basic components of a *keiretsu* (Gheorghiu, 2013) are represented usually by a bank and a foreign trade enterprise. Banks, through their experts, have a big influence in investment projects, through the feasibility studies they make and the granting of preferential loans, when necessary. These financial institutions accept even the prospect of lower profits and dividends, given the long-term success of their investments. Even if *Keiretsu* pay small dividends to shareholders, the tendency is to recapitalize profits by investing in advanced equipment, research and development activities and acquisition of new properties, which in time will reward the sacrifices initially made.

An important characteristic of keiretsu is the practice of cross ownership of shares by the companies that are group members in order to prevent the taking over of the majority of shares and control of the group by foreign companies.

Another significant feature of keiretsu system is the character of unity, manifesting itself in extremely strong and durable personal and business relationships. First, employees show a particular devotion to the group and have the tendency to remain faithful to it throughout life. Typically, in case of regression in business, dismissals are avoided by directing employees towards more prosperous departments of the system. Secondly, the solidity of these business relationships inevitably lead to true personal relationships based on mutual trust between the group and its trading partners. The Japanese distribution system was sharply criticized along time due to"itten itchoai" system that restricts relationships between retailers and wholesalers, with negative effects on competition.

Figure no. 3 – Japanese Model



Source: Interpretation after the following book: Fernando, 2006, p. 54.

3.4 Islamic Model of Corporate Governance

According to this model, good corporate governance is not simply about corporate excellence, it is the key to economic and social transformation. Based on the Koran, in the corporate governance system, both managers of companies as well as the auditors should perform their professional duties, having as a final objective the satisfaction of shareholders' needs and the will of Allah. Thus, corporate governance is aimed to increase accountability, transparency and trust, these values being extremely important in Islam.

As shown in Figure no. 4, corporate governance principles on which the Islamic model is based are (Lewis, 2001):

- Accountability - according to this principle, Muslims believe that they will be held accountable for everything they do in life and in the afterlife. Thus every action must be consistent with Islamic teachings without the existence of fraud or misstatements that may be reflected in their behavior.
- Transparency - the corporation is responsible for a wide spectrum of stakeholders, and for this reason it is obliged to provide clear and accurate information about its policy, since integrity and honesty are the basic features of this type of management. Thus, by applying the concept of transparency, the company should disclose information on its policy, the activities undertaken, its contribution to the community, the use of resources and environmental protection.
- Fairness - Islam supports collective decisions making, tolerance and political freedom. Thus, when making a decision, Muslims put their trust in Allah.
- Responsibility - according to this approach, everyone in the organization must comply with ethical conduct in the exercise of commercial activities. The leader should be judged by how well he manages the company based on Islamic principles, not by how much the wealth has increased.

Figure no. 4 – The fundamental pillars of corporate governance in the Muslim vision

Source: Own processing.

In the case of stakeholders' model, but from the Islamic perspective, managers are required to conduct the business in the interests of all stakeholders. However, each stakeholder has the freedom to protect his rights through systematic institutional arrangements in order to resolve conflicts of interest. Apart from regulatory approach to corporate governance, Islamic beliefs are considered a model of self-regulation, with fear of responsibility before Allah on the Day of Judgment or even during one's life. In spite of these religious restrictions, the principle gives freedom to human beings on how to comply with it while performing their daily chores.

In conclusion, Islamic principles of corporate governance determine three dimensions of decision-making: "by whom", with the mutual consultation of the Advisory Board, "for whom", having as ultimate goal to win the grace of Allah, and not least "with whom and to whom" dimension, i.e. corporate governance decisions require an effective religious supervision to ensure that the operations and procedures comply with the rules of the Koran. Secondly, Islamic instructions for Muslims suggest teamwork and also reflect the fact that team members must follow the command of group leader, whether CEO or Chairman of the Board. Thirdly, the prophet's life is a model of running a business in an Islamic state, whether in wartime or peacetime, which can be considered a procedure in determining the corporate strategy.

4. Results and interpretation

As it can be seen from the above mentioned information, there are some different corporate governance systems. Therefore, we will attempt a comparative analysis of them, by highlighting the similarities and differences between those models.

Thus, as shown in Figure no. 5, we can note that the Anglo-American model is focused on the capital market around which revolves a large number of listed corporations. In turn, the credit institutions role is limited compared to the one played in the Japanese and German models, which are centered on the banking market both in terms of financing and the participation and exercise of control in the process of governance.

We can also notice that specific for the USA and Great Britain is the shareholders type of corporate governance, in which the attention is focused on maximizing the shareholders' profit, while in Germany and Japan the stakeholder type models are more concerned about all the parties interested.

As regards the structure of shareholders, in the countries with long history of corporate governance a dispersed ownership is encountered, a diffuse ownership that does not allow any notable control on the corporation, the latter task being entrusted to managers. On the other hand, in Germany and Japan, the structure of shareholders and thus the ownership and control are concentrated.

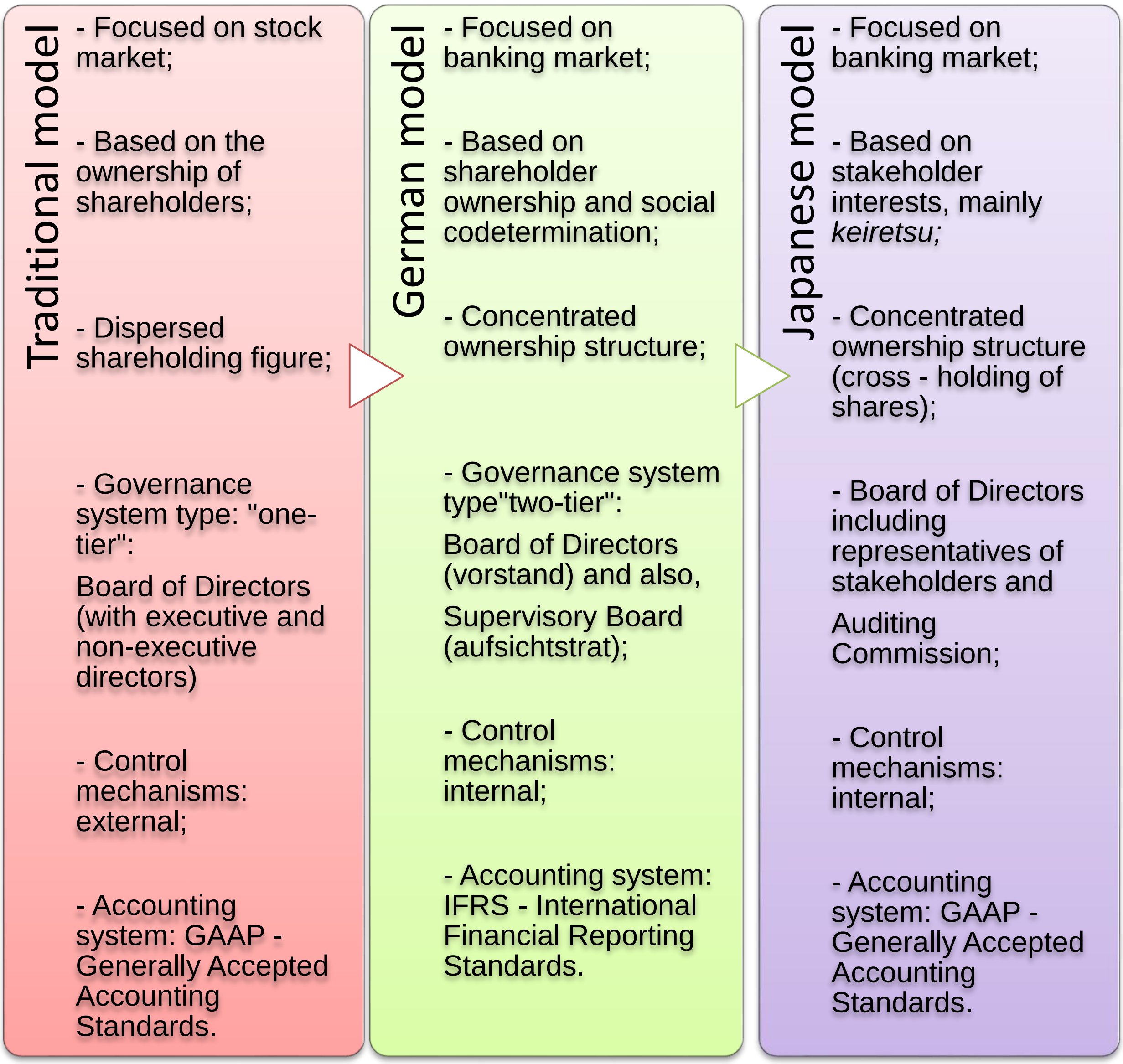
In the Anglo-American model, governance is ensured by the fundamental body, a.k.a. Board of Directors composed of the executives and non-executive directors (in the UK) or outside directors (in the United States). In the German model, governance is ensured by the Vorstand (Board of Directors) - with role of leadership and management and the Aufsichtstrat (Supervisory Board) - with control attributions. In the third model, the Japanese one, the structure of Board of Directors gives a great deal of importance to the interested parties (stakeholders).

German and Japanese corporate governance models are based on internal control mechanisms justified by the existence of strong shareholders such as credit institutions, while the Anglo-American model relies on external control mechanisms under the strong influence of capital markets.

In terms of mobility of employees, in Anglo-Saxon countries there is a flexible labor market which allows an easy transfer from one job to another. In contrast, there is a conservative tendency and a rigid labor market in Germany and Japan that is hampering the mobility of employees; this aspect is justified by the significant investments that employers directs towards the training of personnel, who thus acquires the skills specific to a particular job and a special attachment to the company.

Also, the comparative analysis conducted proves that there are a multitude of similarities between German and Japanese model and especially between the British and American system of corporate governance, and also some distinctive elements for each model.

Figure no. 5 – Comparative analysis of corporate governance models



Source: Own processing

Also, according to the Islamic model, the focus is on ethical values of corporation, on society and on economy. Thus, the benefits of good corporate governance on the corporation are the following:

- ✓ Increasing firm value
- ✓ Lowering cost of capital
- ✓ Enhancing capital efficiency
- ✓ Protection of shareholder’s rights.

On the other hand, if we look through the perspective of economy, the benefits of corporate governance are:

- ✓ Revitalizing market economy
- ✓ Sustainable economic growth
- ✓ Positive development on capital market, more globally competitive
- ✓ Increasing competitiveness through fair competition.

Over time, globalization has resulted in mitigating differences on the implementation of corporate governance models in emerging economies compared to those applied in advanced economies. However, we are still far from talking about a unified approach, taking into account the specificities of each country, and even more the differences between the two categories of economies. We believe that although it is now possible to identify a number of common elements between the different models of corporate governance, there cannot be yet considered in the foreseeable future the idea of a single model of corporate governance perfectly balanced, with consistent application worldwide, due to the socio-economic and cultural differences between countries and the period of uncertainty we are going through.

5. Conclusions

In my opinion, the corporate governance should be based on clear instruments of control and verification of the well defined objectives, which must be measurable, understandable, accurate and consistent with the company's policy. In this respect, an important aspect for both management and shareholders is the verification of the achievement of objectives and therefore, of the performance, both the managament and the company as a whole.

Referring to the case of Romania, corporate governance has emerged beginning with the early 2000s. The delay is explainable by the difficult steps taken on the line of political, legal, economic and social reform. In recent years, however, the corporate governance environment in Romania has changed. Transparency and accountability have become key factors not only for shareholders, but also for investors, buyers, suppliers, and other stakeholders.

As Romania integrates into the global economy, in general and in European Union economy especially, Romanian companies are facing up to the need to compete in a global market place and European market place where investment criteria are increasingly being scrutinized. The volatility that shook the global economy in general and the subsequent impacts on global finance and investment behaviour has amplified the value of good corporate governance for Romanian companies and for sustainable economic development.

Romania has made significant progress in corporate governance during the last two decades, but a number of issues remain. For example, focusing on risk, audit, and other matters have been established by law but, in many cases, have not played their part because of a compliance-oriented business culture. In some cases, independent directors' views are not valued, and benefits of an effective board, especially in the areas of strategic oversight and control, remain unrecognized. Also, the market reflects some special issues of the Romanian firms concerning the capability of being oriented to the objectives. Because of economic instability, the lack of legal framework, the bureaucracy, the excessive tax and control systems, the insufficient sustainability and the financial problems reveals that the Romanian firms are focused on the small and medium terms activity and not to long terms. In the same time, the managers find some solution in order to respect de principles of corporate governance (competitiveness, efficiency, open market) and have developed new products and new technologies.

6. Acknowledgement

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