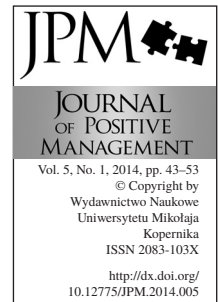


CORPORATE GOVERNANCE AS A CONCEPT IN EVOLUTION (THE CASE OF POLAND)

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Abstract

Purpose: This paper is devoted to the evolution of corporate governance solutions. Its aim is to analyse global, mainly Anglo-Saxon, and German experience in the field of corporate governance, and then attempt to answer the question to what extent this experience can be used in the countries of Central Europe like Poland.

Approach: In the first part of the paper the author conducts a review of the world literature and presents the most important conclusions from the discussion on the need for changes in both concepts: Anglo-Saxon and German. Based on this analysis, the author pointed out possible directions of changes in the Polish solutions.

Implications: The author suggests that the Polish corporate governance does not correspond to the present changes in Western solutions in this area.

Keywords: corporate governance, monistic and dualistic systems, commercial corporations code

Paper type: General review

1. Introduction

Even a brief analysis of corporate governance concepts around the world shows the variety of the solutions used and, at the same time, differences between them. These differences apply almost to everything: legal, economic, and social systems, the nature and role of corporations in the economy, as well as systems of management and control over corporate operations.

The above leads to the conclusion that institutional and structural solutions with regard to corporate governance have an individual nature and are deeply embedded in the economic tradition and corporate culture of a given country. Corporate governance, as yet, does not have a single, widely accepted theoretical base or a commonly accepted paradigm (Tricker, 2009; Horn, 2012). Thus, each country should develop its own approach and solutions in this field using, of course, experience from other countries or regions. The purpose of this study is to identify directions with regard to improvement of the corporate governance

models currently dominant around the world, and then on this basis to provide an answer to the question: what should be implemented or modified in institutional and structural solutions in this field in developing countries like Poland. Needless to say, this issue has the strong impact on the development of Positive Organisational Potential (POP) in every corporation. According to the experts (Glińska-Noweś and Stankiewicz, 2013; Haffer, 2013) corporate governance is one of the key areas of POP. The effective development of this area is impossible without critical reflection based on a review of the world literature.

This paper is a part of broader research project financed from governmental funds (by the National Science Centre) and implemented in the period of 2011–2014. It is devoted to the evolution of corporate governance solutions. Its aim is to analyse global, mainly Anglo-Saxon, and German experience in the field of corporate governance, and then attempt to answer the question to what extent this experience can be used in the countries of Central Europe like Poland.

2. The process of evolution of the Anglo-Saxon and German concepts

Corporate governance is defined as the structure and processes between the board of directors (or supervisory board), shareholders, top managers, top managers and other stakeholders, and involves the roles of the strategic leadership, and the objectives of assuring accountability and improving performance (Shleifer, Vishny, 1997; Cadbury, 2002).

Comparing the Anglo-Saxon and German solutions, which are of greatest interest to us, the first factor that differentiates them is the level of corporate ownership concentration. The Anglo-Saxon models are characterized by dispersed ownership, while the German and Latin models by ownership concentrated in the hands of several shareholders (blocks of shares or votes). This is the result of the presence or absence of some relevant legal regulations. Certain legal restrictions, e.g. the American investment limits with regard to holdings, shape specific ownership structures in corporations. A lack of such limits, e.g. in the case of German banks, leads to their dominance in the ownership structures of local corporations, and, indirectly, to a high degree of concentration of ownership in these corporations. However, it is necessary to point out that concentration of corporate ownership is not an unambiguously negative phenomenon as there is no strong empirical evidence that corporations with concentrated ownership structures, e.g. German, French, or Japanese, are less effective than those with dispersed shareholder structures, e.g. American, British, or Australian.

The second factor differentiating the Anglo-Saxon model from the German one is the structure of shareholders. Individual shareholders are in the minority in all regions of the world. As a result of the process of institutionalisation of corporate ownership, which has been progressing since the mid-1970s, institutions such as pension funds and investment funds have come to be the holders of the

largest blocks of shares in Anglo-Saxon corporations. On the other hand, in German and Japanese corporations this role is performed by banks, insurance corporations and holdings. In the Latin model, significant shareholders are also families and governments. In continental Europe and Japan the institutionalization of ownership is additionally reinforced by so-called mutual or cross ownership, which is supposed to expand and strengthen influences of holdings as shareholders. The institutionalisation of shareholder structure should be regarded as one of the most important features of contemporary corporate governance. It brings about important changes not only in the ownership structures of corporations but also in the systems of supervising and managing their operations. In the mid-1990s these changes were significant enough to gain a special name: investor capitalism.

Any discussion of the advantages and disadvantages of particular models of corporate governance must necessarily address the monistic and dualistic systems of governance. The monistic, or one-tier, system practiced in Anglo-Saxon and Japanese corporations as well as in most French corporations concentrates the management and supervisory functions in the hands of one body referred to as the board of directors. The board of directors usually consists of two groups of members, namely those taking an active part in the corporation's management processes (so-called internal directors) and those performing only supervisory tasks (external directors). Some managerial functions may be delegated to other employees of the corporation who are not members of the board of directors. Such staff members are usually defined as corporate officers. They, however, do not form a separate managing body. On the other hand, the dualistic, or two-tier, system is popular in the prevailing part of continental Europe, and clearly distinguishes the supervisory function, which is performed by a separate body, known as the supervisory board (German *Aufsichtsrat*), while the management function is performed by the management board (German *Vorstand*). Both bodies operate alongside and none of them can issue binding commands to the other. Their mutual impact is, however, quite evident – e.g. it is usually the supervisory board that appoints and dismisses the corporation's management board and determines the remuneration of its members. In addition, under the dualistic system the articles of association of many corporations obligate the management board to obtain consent from the supervisory board to perform some legal actions, e.g. enter into specific transactions. On the other hand, the supervisory board is strictly dependent upon the management board in terms of the quantity and quality of information communicated about the corporation.

The dualistic system, practiced mainly in Germany and Austria, and optionally also in France, is often criticized exactly for this reason, that is, due to the fact that complete knowledge about the corporation is not guaranteed to the persons performing the supervisory functions. These persons, coming from outside the corporation and not having exact knowledge about it, cannot effectively monitor

and control the operations of the management board or provide advice to it. Supporters of the dualistic system emphasize, however, that persons from outside the corporation, having their own managerial or office experience, are able to more objectively look at the activities of a given corporation and, being independent, better represent the interests of the shareholders and more carefully determine the remuneration of management board members. In addition, as independent persons, they may become experts in performing supervisory functions. Finally, in Germany, a separate supervisory body is a platform for cooperation between the representatives of the investors and employees (the co-determination principle). On the other hand, it is difficult not to agree with the supporters of the Anglo-Saxon model that the monistic system has a great advantage in that it provides members of boards of directors performing supervisory functions with full knowledge about what is happening in the corporation and ensures hands-on monitoring of the situation.

A very convincing proof for this advantage has been provided by the decision-making process in the Daimler-Benz/Chrysler merger. This case shows that the role of the supervisory board in Daimler-Benz AG, which is the greatest German industrial group (Neubauer, 2000), is purely perfunctory. Therefore, E. Berglöff and E.L. von Thadden are right in saying that the two-tier system of corporate governance, that is, the separation of supervision from management, increases the power of managers and expands their influence through a broad informal network of various relations (extensive management networks) (Berglöff and von Thadden, 1999).

The excessively strong position of management boards in German corporations, their close connections with suppliers and banks, and, at the same time, the weak position of local supervisory boards arouses anxiety among German investors, who are becoming increasingly influential by the year. Similarly, in other countries associations of investors demand greater transparency and improvement in internal control systems as well as effectiveness from corporate management staff. According to some authors, German corporations and German management are gradually becoming “Americanized” (Schlie and Warner 2000). This applies in particular to large German corporations operating in international markets, such as e.g. Daimler-Benz, Hoechst, Bayer, BASF, Bertelsmann Siemens, Thyssen-Krupp, and Deutsche Bank. These corporations have adapted the American philosophy of managing value for shareholders, with the market price of shares being an important determinant of their effectiveness. They communicate to their investors such important information as the anticipated future profits and dividends. They apply the commonly adopted measures of profitability such as return on equity (ROE) and return on capital (ROC). In addition, they use modern forms of motivating managers (e.g. share options), and send outstanding young managers to do MBA studies in the best American business schools. Finally, these

corporations take an active part in mergers and takeovers as well as implement the international accounting standards (based on the American model), and their business language is English. All of these actions result from the presence of the largest German corporations in the international capital markets, including the New York Stock Exchange.

The above leads to the conclusion that German corporate governance tries to face up to the challenges related to the processes of globalization of business operations. This openness may give rise to an interesting combination of the American idea of value for shareholders with the German ideas of social dialogue, social balance and corporate social responsibility. Such a combination may become a model for other countries of continental Europe, including Poland.

The above comparison of the two most popular models of corporate governance proves that none of them is an ideal solution. On the contrary, each of them has many weaknesses or flaws caused by the opportunism of managers, members of supervisory and executive bodies, or the dominant shareholders. These flaws most often occur due to causes of ethical nature. Nevertheless, to prevent them some institutional solutions have been established or improved in all models with a view to eliminating harmful behaviour against the corporation as a separate economic entity, and in particular against its minority shareholders.

3. Implications for building a modern concept of corporate governance

It is interesting that the vast majority of such changes follow the same direction, regardless of the implemented corporate governance model. The most visible changes showing this convergence are the following:

- Strengthening the role of boards of directors (supervisory boards) as strategic partners for corporations' boards (Stiles and Taylor, 2002). This is caused by the progressing institutionalization of corporate ownership, and consequently, a return to the traditional, active role of shareholders in corporations (investor capitalism). The second factor strengthening the role of the boards is related to sudden bankruptcies and corporate scandals in many countries (the United States, Japan, Germany, France, Italy, Great Britain). They attracted the attention of investors and the general public to the monitoring and control functions of the boards as well as their key role in assessing the quality of the corporation's management. Instead of boards formed by managers, that is, by the people being controlled, it is stressed that the boards need to be treated as an extension of shareholders, or as guardians of the interests of all shareholders, not excluding the minority ones. It is worth emphasizing that reinforcement of the independence of boards and their pro-investor orientation widely discussed not only in Anglo-Saxon countries, but also in Japan and Germany. For example, in Germany the boards have so far mostly cared about the interests of major shareholders and employees, but now a growing importance is given to the interests of the minority

shareholders. Following this, the quality of financial statements as well as other information related to corporation operations is improving (Witt, 2000).

- The most important factor strengthening the role of the boards in the Anglo-Saxon model is independence of the so-called external directors, that is, the group of board members who deal with supervisory activities. In the case of the monistic system, what is mainly at stake is independence from the CEO and other top-level managers. On the other hand, in the dualistic system, the focus is on independence from major shareholders. The advisory corporation KPMG has carried out a study to clarify the notion of independence. A survey conducted among board members of 213 European corporations found that 87% of the surveyed considered a lack of financial and business connections between board members and management the most important criterion of independence (*Corporate ...*, 2002).
- An important element of strengthening the position of the boards is separation of the function of the chairman of the board of directors and the CEO. This applies in particular to American corporations, as in British corporations these two positions have been usually kept separate for many years now. Therefore, the American model is to some degree getting closer to the over 100-year-old idea present in German corporate governance concerning the separation of the supervisory function from the managerial function in a corporation.
- A solution strengthening the role of boards and recommended both in monistic and dualistic systems is appointment of committees. These are most often designed for audit, nomination, and remuneration issues, and often also for executive matters (being involved in the preparation of the board's position concerning the key decisions of the corporation's management) or financial matters (in the case of large international corporations running various investment projects and requiring extensive capital commitment). According to the formulated recommendations, audit and remuneration committees should be formed only of independent board members.
- Another postulate formulated both in monistic and dualistic systems is to treat the board of directors and the supervisory board as strategic resources of the corporation. The board, and in particular its appropriately appointed external members, may be the source of specialist knowledge as well as rich business experience as well as a source of valuable contacts. A concept of the supervisory board which effectively cooperates with and supports the board of directors, especially with regard to strategic decision-making, involves the so-called resource-based trend in company management. This also means seeking a balance between, on the one

hand, monitoring and supervision over the management board's work and, on the other hand, cooperation with and advising the management board.

- Finally, an extremely important factor common to all models of corporate governance is the formulation of codes of good corporate practices. The initiative started in Great Britain in the early 1990s as a result of the well-known report by A. Cadbury (Cadbury, 2002). It has become a platform for building a world standard with regard to corporate governance, among other things, in terms of systems of informing investors, principles of protecting the capital minority, organizing general meetings of shareholders, as well as the work of supervisory and management boards.

The aforementioned changes in the models of corporate governance show that we are witnessing a slow convergence of these models. Of course, these processes are occurring gradually and at least in the nearest future the specific nature of national corporate governance models will be preserved, an example here being the German and Japanese models. Just as J. Lorsch has envisaged, with the deepening globalization of business operations, corporations themselves, their governance systems, and their management and control practices are becoming global (Lorsch, 1997).

Summing up, it has to be said that the process of convergence of various corporate governance models, which is observed around the world, is increasingly evolving in the direction of the Anglo-Saxon model. This phenomenon is also visible in continental Europe, where the German model is preserved in the formal-legal sense only in a few western countries (Germany, Austria, the German-speaking part of Switzerland). It must be added that this model is also changing, gradually absorbing some elements of the Anglo-Saxon model.

4. The Polish corporate governance model – directions of changes

The existing principles of functioning of joint stock corporations in Poland are based on the German model and were written down in the form of a code in the mid-1930s. Pursuant to the essence of the German model, they stipulate the separation of managerial functions from supervisory ones in running a corporation. Thus, the management body, (the management board) independently manages the current operations of a corporation and represents it outside. The competences of the management board include all rights which are not reserved for other corporation bodies under the provisions of the Polish Commercial Corporations Code (*Act of 15 September 2000 – Commercial Corporations Code 2003*) or the corporation's articles of association – this is the principle of presumption of competences of the management board (Softysiński et al., 2008). Members of the management board are required to ensure the proper operation of the corporation, in accordance with its purpose and object of operations specified in its articles of association, and

at the same time demonstrate due diligence – to an extent higher than generally required. This diligence should arise from the professional nature of operations of the corporation’s administrator – Article 483, § 2 of the Polish Commercial Corporations Code (Sołtysiński et al., 2008).

Along with the management board, a body which is obligatorily appointed in Polish corporations is the supervisory board. The main task of this body is to carry out permanent supervision over the corporation’s business in all fields, including supervision over the corporations run by the corporation.

Like the management board, the supervisory board performs its activities jointly, which means that they are reserved for the whole board as a corporate body. For practical reasons, the board may, however, authorize its member or members to perform specific activities by means of a resolution. The board may also appoint committees or commissions from among its members and authorize them to perform supervisory activities in a given field of the corporation’s operations. Positions on specific matters should, however, be agreed by the board jointly.

It is extremely important to stress that, in accordance with the new Article 375 of the Commercial Corporations Code, the supervisory board is not authorized to issue to the management board any binding commands concerning corporation matters. Therefore, the rights of the management board and the supervisory board are clearly separated, emphasizing that the management board works within the scope of its rights independently and is not subordinate to the supervisory board (Sołtysiński et al., 2008).

In our opinion, the decision included in Article 375 of the Commercial Corporations Code is an expression of excessive faith in the power of managers, which E. Berglöf and E.L. von Thadden warn against (Berglöf and von Thadden, 1999). This deepens the dualistic character of Polish corporate governance, and, as a consequence, reduces mutual trust as well as hinders cooperation between a corporation’s management board and supervisory board. Furthermore, this solution is not in line with the spirit of the latest tendencies in reforming corporate governance in the world, in particular in the so-called post-Enron age following the management abuses and corporate scandals that took place in the early 21st century in the United States and Europe. The answer to these phenomena is to strengthen the position of management boards and supervisory boards, extending their activity not only with regard to the control function, but also the advisory function – in accordance with the common belief that the board is a strategic resource of the corporation that should be used by managers in strategic management processes.

It is also necessary to remember that supervisory boards in Polish corporations have a slightly weaker formal and legal position than those in German corporations, operating under the same system. In the German commercial law, like in the Polish

case, supervisory boards jointly approve some specific actions of management boards. In German corporations, the list of these activities is, however, generally quite long. For instance, it applies to important investment projects, purchasing or disposing of real estate, taking loans above a specified amount, granting loans or credit guarantees to other entities, undertaking restructuring projects on a large scale, opening or closing representative offices or plants, undertaking a new type of activity, purchasing or selling shares, employing or dismissing high-ranking employees, and granting powers of attorney (Hoffmann 1985: 69; Striebeck 1992). A list of decisions subject to approval may be even longer and is determined by the corporation's articles of association or by the board itself in the case of a vital interest of the corporation (management boards may not appeal such decisions of supervisory bodies to general meetings of shareholders). In contrast, Polish supervisory boards are unable to extend their control rights (Article 391, § 1 and 3 of the Commercial Corporations Code) as this type of change would each time require a corresponding change in the articles of association, which belongs to the competences of the general meeting of shareholders. Furthermore, when the supervisory board of a Polish corporation refuses to perform a given activity listed in the articles of association, the management board may apply for approval to the general meeting of shareholders (Article 384 § 2 of the Commercial Corporations Code). It is beyond doubt that these solutions put Polish supervisory boards in a significantly worse position than those in German corporations.

Looking at all the regulations contained in the Polish Commercial Corporations Code, the most significant changes include regulations concerning mergers, divisions and conversions of corporations. These problems, which are of growing importance for the developing Polish economy, did not have a sufficiently mature legal base in the "old" commercial code. Thus, one should agree with the opinion of W.J. Katner and co-workers that the current Polish Commercial Corporations Code in this field meets the new needs of economic activity (Katner 2006: 137).

5. Conclusions

The selected areas of Polish corporate governance presented above are obviously not exhaustive in view of the entire problem. If one needs to adopt a more holistic approach to this subject (Hardi and Buti 2012), one should take into account the following elements: trade in securities, accounting and the principles of preparing and publishing financial statements, as well as external and internal audit. However, the adopted system of corporate governance has a fundamental importance for the business effectiveness of corporations. The dualistic system – which is still in existence in the Polish Commercial Corporations Code – is clearly losing some of its importance not only around the world, but also in continental Europe. A convergence of the monistic and dualistic systems that has been visible

in Europe for some years now as well as the evolution of the dualistic system in Germany should become an impulse for departing from the existing, conservative approach to the separation of managerial and supervisory functions in the Polish commercial law.

After all, one cannot ignore the fact that the monistic system is the absolutely dominant solution in the world and that it is clearly associated with the process of globalization of the world's economy. In addition, some major countries in continental Europe are withdrawing, or have already withdrawn, from the dualistic system (e.g. the Nordic countries), while others, like e.g. France, have granted corporations the right to choose a governance system. One of the intentions of the European Commission is to prepare a directive obligating the member states to allow public corporations to make such a choice. Therefore, the question arises as to the point of further preserving the division between managerial and supervisory functions, since more than a century of practicing this system has demonstrated no superiority of the dualistic system over the monistic one. Furthermore, this system seems to cause substantial dissatisfaction even in Germany. In any case, the reform of corporate governance in Poland and other Central and Eastern European countries should become the subject of a major discussion among economists, lawyers, and politicians.

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