Comparative Analysis of the Corporate Governance Rules (Germany-Romania)

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Abstract

This paper focuses on the Corporate Governance Rules in two European Member States, Germany and Romania. The paper only addresses the listed stock exchange companies that should abide the Corporate Governance Codes that exist in both countries and focuses on the articles of the Codes.

Germany as an OECD member state, has a Corporate Governance Code, whereas Romania is not yet a member and has no Corporate Governance Code issued by the legislator. The hypothesis of this paper is the fact that the two codes are similar, and by this I mean that Romania derived part of its code from the German one. The only Corporate Governance Rules that must be followed in Romania are the ones contained in the Bucharest Stock Exchange Corporate Governance Code, for the Romanian listed companies.

The comparative analysis of the two Corporate Governance Codes reveals similarities and differences that will be discussed in this paper.

To respond to the international market and attract foreign investors, both systems must accept and apply the corporate governance rules that exist, taking into consideration the OECD principles.

Contents

Introduction

To achieve a socially acceptable status in which we care for the greater good we need Governance, this takes me to the Greek people which gave us Democracy.

In the 21st century that we live in, a significant part of the wellbeing of the economic systems that exist worldwide relies on corporations.

Corporations are everywhere and some of them have a lot of financial power and it could happen that they are more powerful than some states in which they do business, and obviously they are run by people. It could also happen that the people managing a company will only be interested in the money making process and they will do almost anything to achieve that goal, that is why we should have rules that will prevent this kind of behavior and help us filter the decisions taken in the day by day life of the corporations that they manage.

In order for a corporation to function properly it needs corporate governance rules. Those rules that were enacted by most states, either through hard law, soft law or suggestions could help the company develop and get the necessary funding for it. We can see how rules that deal with corporate governance apply worldwide and in my opinion the faster we understand that we should think locally and act globally the better.

Whether we take into account developed economies or emerging ones, Corporate Governance Rules should exist and they should be taken into account. I make this statement because among others it is of paramount importance for companies in every state around the world to be able to get capital from the international markets.

There are many analyses available that were made between countries with regards to their Corporate Governance Rules, but I think this one is important because it compares one of the world leading economies, Germany, that has a well-developed business culture with an emerging democracy and a new comer in the European Union, Romania.

Corporate Governance is a vast domain and for the purpose of this paper I will only analyze the companies that are listed on the stock exchanges, otherwise this would transform into a paper for a Doctoral thesis that will need the three years of the program to write it.

Every year there are corporate scandals around the world, and because the field is not that well developed, like criminal law for example, corporations manage to show the legislator wrong doings before it can react. This is why every piece of legislation comes after a huge scandal[1].

The purpose of the present paper is to provide a glimpse on the similarities and differences that exists in the two countries with regards to the Corporate Governance Rules.

In this paper i will talk about the Corporate Governance concept, about the context in which it emerged and the cases that made this rules become necessary. We should always have rules to protect us is in our day to day life, otherwise the famous cases that led to the creation of the Corporate Governance rules could repeat themselves.

In chapters 2 and 3 I will analyze the Corporate Governance Rules in two of the European Union Countries. The first country to be analyzed will be Germany that has a well-developed corporate systems and strong corporations that started acting in the international market decades ago. I will write about the development of the Corporate Governance, describe specific provisions, then analyze the German Corporate Governance Code and in the end talk about a famous case.

[1] Enron in the United States, Holzmann in Germany .

The second country to be analyzed will be Romania, which became a member of the European Union approximately 8 years ago. The Corporate Governance Rules were introduced later than the German ones, so there were existing models for the rules from which they could have inspired. I will also discuss the specifics of the rules and point out an important case.

The last part of this paper will be the Conclusion chapter in which we will discuss similarities and differences between the two countries. My hypothesis is that the Romanian model was inspired from the German one.

The methodology that I will use is a comparative analysis, comparing the pieces of legislation available in the two countries.

As a practical application of this paper, you will know what are the similarities and differences between the Corporate Governance Rules in the two countries from a legal point of view and I will also describe some cases in which the Rules were disregarded. After reading this paper and the conclusions you will understand the need to have a Corporate Governance Code in Romania issued by the legislator not by the Stock Exchange.

Chapter 1 - Corporate Governance

Corporate Governance is a relatively new concept, which started to be developed after big companies failed[2]. This concept represents the "rules of the game" that are used to manage a corporation and protect the shareholders rights[3]. By using this rules that should be generally understood and available in multiple languages it is much easier to attract investors.

1.1 Definition and Principles of Corporate Governance

Democracy is a form of government in which the power is vested in the people and exercised by them directly or by their electoral agents[4]. Corporate governance is similar to this notion.

Corporate Governance can be defined in at least 3 ways:

The OECD defines Corporate Governance as "Procedures and processes according to which an organization is directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among the different participants in the organization – such as the board, managers, shareholders and other stakeholders – and lays down the rules and procedures for decision-making"[5].

In a business newspaper called The Economic Times we find another definition:

> Corporate governance refers to the set of systems, principles and processes by which a company is governed. They provide the guidelines as to how the company can be directed or controlled such that it can fulfill its goals and objectives in a manner that

[2] WorldCom, Parmalat, Enron *id.*
[3] Niculae FELEAGĂ et al., *Corporate Governance in Emerging Economies: The Case of Romania*, 9 THEORETICAL AND APPLIED ECONOMICS 5, 1 (2011).
[4] Dictionary definition, available at http://dictionary.reference.com/browse/democracy accessed on 11.02.2015
[5] OECD Glossary of Statistical Terms , available at http://stats.oecd.org/glossary/detail.asp?ID=6778 accessed on 11.02.2015

adds to the value of the company and is also beneficial for all stakeholders in the long term.[6]

Finally, a dictionary called USLegal describes Corporate Governance as "A generic term which describes the ways in which rights and responsibilities are shared between the various corporate participants, especially the management and the shareholders"[7]

For the purposes of this paper we will refer to Corporate Governance as being a set of principles by which a company is governed.

Principles of Corporate Governance[8]

The Corporate Governance Principles are focused on publicly traded companies but they can also be used to improve Corporate Governance in non-traded companies, and they are used as a guide by all the states that use Corporate Governance rules[9]. I will quote the OECD principles and enter a few comments of my own; this is important because Romania is not a member of the OECD while Germany is a member of OECD.

Principle 1 – Ensuring the Basis for an Effective Corporate Governance Framework

> The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory, and enforcement authorities.
>
> A. The corporate governance framework should be developed with a view to its impact on overall economic performance, market integrity and the incentives it

[6] What is corporate governance?, http://articles.economictimes.indiatimes.com/2009-01-18/news/28462497_1_corporate-governance-satyam-books-fraud-by-satyam-founder accessed on 11.02.2015.
[7] Corporate Governance Law & Legal definitions , available at http://definitions.uslegal.com/c/corporate-governance/ accessed on 11.02.2015
[8] OECD, OECD Principles of Corporate Governance (2004), http://www.oecd.org/daf/ca/corporategovernanceprinciples/31557724.pdf.
[9] *Id.* at 11.

creates for market participants and the promotion of transparent and efficient markets.

B. The legal and regulatory requirements that affect corporate governance practices in a jurisdiction should be consistent with the rule of law, transparent and enforceable.

C. The division of responsibilities among different authorities in a jurisdiction should be clearly articulated and ensure that the public interest is served.

D. Supervisory, regulatory and enforcement authorities should have the authority, integrity and resources to fulfill their duties in a professional and objective manner; moreover, their rulings should be timely, transparent and fully explained[10].

It should be in the interest of every state and corporation to comply with this principle, because we live in a world in which borders disappear and in the present market setting it is very easy to become interesting for a foreign investor. In order for this to happen, law makers should try to implement this principle in the best possible way.

Principle 2 – The Rights of Shareholders and Key Ownership Functions

The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

A. Basic shareholder rights should include the right to : 1) secure methods of ownership registration; 2) convey or transfer shares; 3) obtain relevant and material information on the corporation on a timely and regular basis; 4) participate and vote in general shareholder meetings; 5) elect and remove members of the board; 6) share in the profits of the corporation

[10] *Id.* at 17.

B. Shareholders should have the right to participate in, and to be sufficiently informed on, decisions concerning fundamental corporate changes such as: 1) amendments to the statutes, or articles of incorporation or similar governing documents of the company; 2) the authorization of additional shares; 3) extraordinary transactions, including the transfer of all or substantially all assets, that in effect result in the sale of the company

C. Shareholders should have the opportunity to participate effectively and vote in general shareholder meetings and should be informed of the rules, including voting procedures, that govern general shareholder meetings (…)

D. Capital structures and arrangements that enable certain shareholders to obtain a degree of control disproportionate to their equity ownership should be disclosed

E. Markets for corporate control should be allowed to function in an efficient and transparent manner (…)

F. The exercise of ownership rights by all shareholders, including institutional investors should be facilitated (…)

G. Shareholders, including institutional shareholders, should be allowed to consult with each other on issues concerning their basic shareholder rights as defined in the Principles, subject to exceptions to prevent abuse[11].

In order to have a functional economy, in which shareholders exist and invest, lawmakers should offer rights and protect them in the best possible way. By doing so, shareholders will invest their money and the economy will grow. Shareholders should be involved in the life of the corporation and should have all the rights described by this principle.

Principle 3 – The Equitable Treatment of Shareholders

[11] *Id.* at 18,19.

> The corporate governance framework should ensure the equitable treatment of all shareholders, including minority shareholders and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.
>
> A. All shareholders of the same series of a class should be treated equally (…)
> B. Insider trading and abusive self-dealing should be prohibited
> C. Members of the board and key executives should be required to disclose to the board weather they, directly, indirectly or on behalf of third parties, have a material interest in any transaction or matter directly affecting the corporation[12].

In the majority of states around the world, equality is a principle which exists in their Constitutions. This principle states the obvious, that everybody should be treated equally in order to prevent abuse and in order to preserve the economy. In my opinion, if the framework would not prevent abuses the immediate effect will be the termination of investments coming from shareholders.

Principle 4 – The Role of Stakeholders in Corporate Governance

> The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporation and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.
>
> A. The rights of stakeholders that are established by law or through mutual agreements are to be respected
> B. Where stakeholder interests are protected by law, stakeholders should have the opportunity to obtain effective redress for violation of their rights

[12] *Id.* at 20.

C. Performance-enhancing mechanisms for employee participation should be permitted to develop

D. Where stakeholders participate in the corporate governance process, they should have access to relevant, sufficient and reliable information on a timely and regular basis

E. Stakeholders, including individual employees and their representative bodies, should be able to freely communicate their concerns about illegal or unethical practices to the board and their rights should not be compromised for doing this

F. The corporate governance framework should be complemented by an effective, efficient insolvency framework and by effective enforcement of creditor rights[13].

Corporate governance framework should be created to protect and encourage the actors involved in this process. Law and other agreements related to corporate governance should offer on one hand a climate in which everybody can express their concerns and not be afraid of the consequences and on the other hand an effective system to solve problems that might appear.

Principle 5 – Disclosure and Transparency

The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership and governance of the company.

A. Disclosure should include, but not be limited to, material information on:

1) The financial and operating result of the company; 2) company objectives; 3) major share ownership and voting rights; 4) remuneration policy for members of the board and key executives, and information about board members,

[13] *Id.* at 21.

including their qualifications, the selection process, other company directorship and whether they are regarded as independent by the board; 5) related party transactions; 6) foreseeable risk factors; 7) issues regarding employees and other stakeholders; 8) governance structures and policies, in particular, the content of any corporate governance code or policy and the process by which it is implemented

B. Information should be prepared and disclosed in accordance with high quality standards of accounting and financial and non-financial disclosure

C. An annual audit should be conducted by an independent, competent and qualified, auditor in order to provide an external and objective assurance to the board and shareholders that the financial statements failry represent the financial position and performance of the company in all material respects

D. External auditors should be accountable to the shareholders and owe a duty to the company to exercise due professional care in the conduct of the audit

E. Channels for disseminating information should provide for equal, timely and cost-efficient access to relevant information by users

F. The corporate governance framework should be complemented by an effective approach that addresses and promotes the provision of analysis or advice by analysts, brokers, rating agencies and others, that is relevant to decisions by investors, free from material conflicts of interest that might compromise the integrity of their analysis or advice[14].

A shareholder that wants to invest his money, needs all kind of financial statements from the company, so that he can be sure that his investment will be protected. This principle helps to set a legal framework that will give the shareholders and others that are interested in the

[14] *Id.* at 22,23.

company information about the financial status of the company. In my opinion the best suggestion given by this principle is the external control and opinions that must be given, in order for investors to take a decision and in order for the state to know how the company is doing.

Principle 6 – The Responsibilities of the Board

> The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.
>
> A. Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders.
> B. Where board decisions may affect different shareholder groups differently, the board should treat all shareholders fairly
> C. The board should apply high ethical standards and it should take into account the interests of stakeholders.
> D. The board should fulfill certain key functions (…)
> E. The board should be able to exercise objective independent judgment on corporate affairs (…)
> F. In order to fulfill their responsibilities, board members should have access to accurate, relevant and timely information[15]

The corporate governance framework should be built in such a way that it should give the board rights and obligations toward the company and the shareholders. In my opinion this principle implies the use of a two tier system because of the wording that it uses.

[15] *Id.* at 24,25.

1.2 History of the Concept of Corporate Governance

The concept of corporate governance had existed since the 16th century when the East India Company was created[16]. The concept started to be used when problems appeared between managers and investors of corporations. In this respect I would say that Corporate Governance is for companies what democracy is for some states, by this I mean that it is important to have equality between the two parties and elections to ensure a democratic rule of the corporation; otherwise we could have abuse coming from the managerial side.

Corporate Governance has become a highly discussed topic in the last 30 years because of the following: the wave of privatization that we can find basically all over the globe; the takeover wave that happened in the 1980's; the deregulation and interrogation of capital markets; a series of corporate failures in the United States[17].

After the Second World War the United States had a big economic growth, and the corporations grew in a very short period of time. In those corporations managers ruled and directors and shareholders followed their lead[18]. The legal statutes that were available at that time offered a very low level of protection for the shareholders, this is one of the reasons why we had the big business failures; the legal framework developed only after something went wrong which showed what was wrong with the existing rules.

Corporate Governance is linked to the United States because, on the one hand, it is the leading capitalist of the world and, on the other hand, it showed the world how things can go really bad if you don't pay attention to what the corporations are doing. In my opinion, the modern legislation that exists today in all the countries around the globe is linked to a major United States corporation called Enron, an energy company.

[16] Brian R. Cheffins, *The History of Corporate Governance*, SSRN Scholarly Paper ID 1975404 1 (Social Science Research Network), Dec. 1, 2011.
[17] Marco Becht et al., *Corporate Governance and Control*, SSRN Scholarly Paper ID 343461 4 (Social Science Research Network), Oct. 1, 2002.
[18] Cheffins, *supra* note 16, at 2.

In 1976, the term Corporate Governance first appeared in the Federal Registry because of an investigation that was conducted by the Federal Securities and Exchange Commission against three outside directors of a corporation called Penn Central[19], a railway company. This company was created after a merger between two companies and the issue here was that, at that time, the law did not require full and complete disclosure of the details of the merger to the stockholders of the corporation. It was at that time the largest bankruptcy in the United States.

In 1981, an advisory committee on Corporate Governance that was composed of representatives of the industry, shareholders and consumers agreed that improvements in the Corporate Governance were vital for the development of the economy but they failed to agree on the legislative acts that should be developed[20] .

In the early 1980's American Law Institute took on the challenge to draft some rules for Corporate Governance with the help of the American Bar Association and the New York Stock Exchange[21]. The law that exists today resembles the Corporate Governance Principles that were issued by the American Law Institute in 1994[22].

The company that I mentioned above, Enron[23], managed the performance to have the biggest recorded bankruptcy in the history of the United States at that time. As we can see from the article that I cited, among the things that led to this bankruptcy was the pride of the managers, excessive risk taking, questionable activities with regards to the energy market, not disclosing information to its shareholders and as an extra their audit and accounting company helped

[19] Penn Central Transportation Company, et al. v. New York City, et al., (United States|US Supreme Court Jun. 26, 1978).
[20] Cheffins, *supra* note 16, at 7.
[21] *Id.* at 9.
[22] *Id.* at 13.
[23] Steven Pearlstein and Peter Behr, *At Enron, the Fall Came Quickly; Complexity, Partnerships Kept Problems From Public View*, THE WASHINGTON POST (2001).

them modify the books in order for them to have a very good financial record even though they were actually losing money[24].

The Corporate Governance principles that were available at that time, were not really taken into account, and as a result after Enron's bankruptcy in 2002 the United States legislator responded by issuing a new piece of legislation called Sarbanes-Oxley Act that tailored the existing corporate governance rules. In addition to this act the New York Stock Exchange also adopted a code for the listed companies called New York Stock Exchange Corporate Governance Rules[25].

In my opinion, all the existing legislation on Corporate Governance exists mainly because of the American Corporations that showed the world the need for additional protection offered by the Corporate Governance rules or principles.

It is my belief that the drafters of the OECD Corporate Governance Principles that were discussed earlier in this paper took into account the American Legal Institute Corporate Governance Principles.

1.3 Corporate Governance in the world

There are several corporate governance models in the world, which differ from each another because of the society in which they are implemented.

The OECD issued some basic principles that have to be followed in order to have an efficient corporate governance, but not all countries are members of the OECD.

In my opinion, among other very good things brought to us by globalization, is the fact that most of the publicly traded companies act in international markets. In order for them to be

[24] *Id.*
[25] Robert Charles Clark, *Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too*, SSRN Scholarly Paper ID 808244 3 (Social Science Research Network), Dec. 5, 2005.

listed they have to comply with the Corporate Governance Rules that are issued by each stock exchange.

For the purpose of this paper we will discuss only three leading Corporate Governance models, the Anglo-American Model and the Japanese Model in this chapter, and the German Model in the next chapter, which focuses on the German Corporate Governance Code.

Anglo-American Model

This model is also called Anglo-Saxon model and the most important countries that use this model are: United Kingdom, United States of America, New Zeeland, Canada and Australia.

Ownership of the corporation is shared by individuals and outside investors called shareholders, which in normal circumstances prefer rather to invest in companies than in banks because of the potential profit that they could make.

In some of these countries, but especially in the United States, equity financing is widely used and there is a strong link between this type of financing and the corporate governance system[26].

The key players in this model are the managers, the shareholders and the directors[27]. The interest of managers and shareholders might not always coincide. Legislators drafted rules requiring the election of the board of directors by shareholders and they also imposed fiduciary duties on the board of directors to supervise the management of the company in the shareholders behalf[28].

There are some interesting facts that I would like to point out in this model of Corporate Governance. One of them is the fact that the shareholders appoint the board of directors which

[26] Terence Mendis, *Analysis of Corporate Governance Theories and Their Implications for Sri Lankan Companies*, JOURNAL OF THE FACULTY OF GRADUATE STUDIES 19, 1 (2012).
[27] *Id.* at 2.
[28] *Id.*

appoints the management of the company. Another interesting fact is that the board of directors is composed of executive directors that are directly employed by the company and non-executive directors which are not in a contractual relationship with the corporation[29].

The last fact that I would like to point out is that they normally use a proxy system to vote, and this seems to be a good solution because the corporation can function and the board of directors can be appointed by the shareholders or their proxies[30].

The United States offered a chance to own a part of the corporation to the general public and on top of this they improved their legal framework every time a flaw was pointed out. This might be one of the reasons why the United States have the biggest capital market in the world and the other might be that by having this kind of corporate governance model they offer democratic rights to the shareholders and the board of directors.

Japanese Model

Equity financing is also important in this model, but the shareholders of the corporations are mainly banks and corporate insiders[31].

This model is very interesting because there are two main shareholders, on the one hand you have the banks[32] that are usually the majority shareholders and they provide it with loans, consulting services and other related services and on the other hand you have the keiretsu which is a network of affiliated companies that use cross-holdings of debts and equity, trading and informal contacts[33].

The main actors in this model are the banks, the keiretsu, the Government and the management which work together for the benefit of the company.

[29] *Id.* at 3.
[30] *Id.* at 6.
[31] *Id.*
[32] *Id.*
[33] *Id.* at 7.

The board of directors is composed almost entirely of insiders. If the company is doing well and it has profit they can be a part of the board for a long period, but if the company's profit diminishes over a certain time period the main bank and the keiretsu will remove the directors and appoint their own directors to govern the company[34].

It is my understanding that the only intervention that might occur in the Corporation's life is when it starts having financial difficulties. For the majority of the countries that have capital markets it is not common to have government officials that sit in the board of directors, but I think that in Japan this is a method that helps the corporation; on the one hand because of the respect that exists in their society and on the other hand because it creates a direct relation between the main actors that are involved in the corporations life.

I described this model, to have a better understanding of the Oltchim case that I will discuss in the 3rd chapter, in which we can see how the state tried to apply this model but had done it in a terrible manner, so that the company which was one of the biggest in Eastern Europe is now insolvent.

Chapter 2 - Corporate Governance Rules in Germany

2.1 History of Corporate Governance in Germany

Before 1990, Germany was referred to as the German corporation, because the companies only used two main sources of funding, retained profits or loans from the banks. The first law that was enacted in Germany was highly protecting the creditors and neglecting the stockholders. This changed after the 1990, firstly because of globalization, secondly because of the competition that existed in the international markets and thirdly because of the liberalization of the financial markets. Initially investors found German companies less

[34] *Id.* at 8.

attractive because of the underdevelopment and lack of transparency of the corporate governance[35].

There was a big insolvency case at the beginning of the year 2000 that involved a famous construction company called Holzmann that filed for bankruptcy in Germany; it is known as the Holzmann insolvency crisis. After this case, the German government understood the practical importance of better corporate governance for the German companies in the competitive international context, and they established several commissions to draft a Corporate Governance Code; the result was the drafting of the German Corporate Governance Code that entered into force in February 2002[36].

In my opinion, the Germans responded to a market reality, because in order to get capital from foreign investors you have to comply with a set of rules which they are used to. Furthermore the Anglo-Saxon corporate governance system influenced the German system, on the one hand because they are the leading capitalists of the world and on the other hand if Germany wouldn't have complied they would have fallen behind everybody else.

2.2 Corporate Governance Rules in Germany

In Germany the most important laws that deal with corporate direction and control are the following:

- The Stock Corporation Act (Aktiengesetz)
- The Civil Code (Bürgerliches Gesetzbuch)
- The Limited Liability Corporation Act (Gesellschaft mit beschränkter Haftung)
- The Commercial Code (Handelsgesetzbuch)
- The Co-determination Act (Mitbestimmungsgesetz)

[35] Gerhard Cromme, *Corporate Governance in Germany and the German Corporate Governance Code*, 13 CORPORATE GOVERNANCE: AN INTERNATIONAL REVIEW 362, 1 (2005).
[36] INSTITUTE OF DIRECTORS, THE HANDBOOK OF INTERNATIONAL CORPORATE GOVERNANCE: A DEFINITIVE GUIDE 192 (Kogan Page, 2nd ed ed. 2009).

- The Securities Trading Act (Wertpapierhandelsgesetz)
- The European Stock Corporation Act (Societas Europeae Ausführungsgesetz)

On top of this framework, Germany responded to the international need and adopted a Corporate Governance Code to which German Stock companies have to comply.

The rules contained in the GCGC are no statutory law but mere soft law. There are concerns with regards to the constitutionality of the code because the code is neither an act of the Parliament nor an agreement that binds various parties[37]. Even though the GCGC offers just recommendations that are not binding by themselves, they are supposed to work as "de facto" rules which will be enforced by the pressure of the capital markets[38].

Since it was enacted in February 2002, the GCGC was amended three times and the goal is to make the German corporate governance system transparent and comprehensible. With regards to the supervision and management of the listed German stock corporations, the code tries to promote the trust of national and international investors, customers, employees and the general public[39].

It is important to know that all German stock corporations have a mandatory two-tier board structure composed of the Supervisory Board and the Management Board.

I will now discuss and highlight some important articles from the latest version of the GCGC:

2.2.1 Shareholders and the General Meeting

As we can see from the text of the article[40], normally every share caries one vote, and the shareholders have the right to exercise it before the General Meeting. In the German legal

[37] Michael Kort, *Standardization of Company Law in Germany, Other EU Member States and Turkey by Corporate Governance Rules*, 5 EUROPEAN COMPANY AND FINANCIAL LAW REVIEW 379, 36 (2008).
[38] *Id.* at 37.
[39] *Id.* at 4.
[40] German Corporate Governance Code Art 2.

provisions it is stipulated that the shares can't have preferential voting rights, multiple voting rights or maximum voting rights[41].

A General Meeting has to take place at least once a year that will be convened by the Management Board which has to give details about the agenda of the meeting. In special cases a quorum of shareholders can demand the convening of a meeting and they can demand the extension of the agenda[42]. Every shareholder has the right to take the floor during the meeting and ask questions and make proposals for the things that are on the agenda[43]. There is a provision stating that the meeting should last at least 4 to 6 hours and in my opinion this is the legislators way of making sure that the meeting is a real one and not fake one in which everybody shakes hands, drink coffee and go on with their business[44]. During this meeting the shareholders representatives to the Supervisory Board are elected[45].

The General meeting deals among others with the Articles of Association, the purpose of the company, can amend the Articles of Association and it also deals with essential corporate measures that will be discussed in the later, by this provision the legislator ensures that every decision is taken by the majority and everybody is or should be informed about it[46].

The Annual Financial Statements, the Management Report, the Consolidated Financial Statements and the Group Management Report have to be submitted to the General Meeting by the Management Board, by doing this the legislator ensures that the shareholders can see relevant data and take decisions on actual performance of the company[47].

[41] *Id.* Art 2.1.2.
[42] *Id.* Art 2.3.1.
[43] *Id.* Art 2.2.3.
[44] *Id.* Art 2.2.4.
[45] *Id.* Art 2.2.1.
[46] *Id.* Art 2.2.1.
[47] *Id.* Art 2.2.1.

The annual report of the company and the date on which the meeting will take place has to be brought to the shareholders attention[48], either by direct contact or by posting it on the company's internet page[49]. It is also stipulated that the company has to ensure the use of proxy voting on top of the exercising of the shareholders individual voting rights[50].

During this meeting it can be decided to issue more shares, purchase existing ones and other financial instruments that could help the financing of the company[51]. In case a decision is taken to issue more shares, the existing shareholders have a pre-emptive right to buy them otherwise their participation in the company could be diluted[52].

2.2.2 Cooperation between Management Board and the Supervisory Board

It is stated in this article[53] that it's in the best interest of the company that the two boards cooperate closely.

For a good Corporate Governance there has to be opened discussions between the two boards on the official level and also between the members of the boards, but confidentiality has to be taken into account[54].

The Management Board takes the crucial decisions directs the corporation in the direction that they want and decide on important issues with regards to strategy, planning, business development, risk situation, risk management and compliance, but they have to discuss it at regular intervals with the Supervisory Board[55]; in my opinion this is one of the main filtering tools offered by the German Corporate Governance Model. If in any case the Management

48 *Id.* Art 2.3.1.
49 *Id.* Art 2.3.3.
50 *Id.* Art 2.3.2.
51 *Id.* Art 2.2.1.
52 *Id.* Art 2.2.2.
53 *Id.* Art 3.
54 *Id.* Art 3.5.
55 *Id.* Art 3.2.

Board wants to change the business plan that was previously agreed, they have to explain why to the Supervisory Board.

There is a provision stating the fact that the Supervisory Board has to make sure that they get enough information from the Management Board and for this to happen they must specify the information and reporting duties of the later[56].

In case the members of the two boards violate the due diligence of a prudent and conscious member of the Supervisory Board and the Management Board they will be liable to the company for damages[57], this provision shows that they also have bigger responsibilities.

Under German law it is mandatory to have a two-tier system when you have a stock corporation; by having a management board that is elected by the supervisory board is in my opinion much better because you can filter the decisions and the shareholders are better protected.

2.2.3 Management Board

Members of the Management Board are the ones that manage the company but they have to take into account also the interest of the shareholders, the employees other stakeholders[58]. They have to make sure on the one hand that the law and the company's internal policies are followed[59] and on the other hand they must ensure appropriate risk management and risk control in the company[60]. There is also a provision stating that diversity should be taken into account when nominating members of the board[61].

[56] *Id.* Art 3.4.
[57] *Id.* Art 3.8.
[58] *Id.* Art 4.1.1.
[59] *Id.* Art 4.1.3.
[60] *Id.* Art 4.1.4.
[61] *Id.* Art 4.1.5.

The Board is composed of several people that are appointed by the Supervisory Board and every company should have by-laws that govern their work[62].

The compensation of the Board is determined by the Supervisory Board based on their performance and also based on the sustainable growth of the company, so even though they are the ones that manage the company they still get paid by their supervisors[63]. In my opinion it is good to have such a provision in the Code, otherwise if things were different they could take advantage of the system and decided to get much more money.

Another provision related to compensation states that the amount given to each member has to be disclosed, so anybody with a legitimate interest should know[64]. The disclosure has to be made in an easy to understand way and it must be done in the Management Report[65], by having this provision the shareholders will know how much do the members make and how much does the company benefit from their work.

It is also stated that they are subject to a non-competition obligation[66], so they are forbidden to demand or accept payments or other advantages[67] that are given for them to act in a detrimental way towards the company.

2.2.4 Supervisory Board

The main task of the Supervisory Board is to advise and supervise the Management Board and they should only be involved in very important business decisions[68]. The members should

[62] *Id.* Art 4.2.1.
[63] *Id.* Art 4.2.2.
[64] *Id.* Art 4.2.4.
[65] *Id.* Art 4.2.5.
[66] *Id.* Art 4.3.1.
[67] *Id.* Art 4.3.2.
[68] *Id.* Art 5.

have the expertise required for the business that they will supervise[69]. The Supervisory Board appoints and dismisses the members of the Management Board[70].

They are elected by the General Meeting of Shareholders, and because of the German Co-determination that will be discussed later in this paper half of them are employee representatives and the other half are shareholders representatives. Before they are elected, they must disclose information about themselves and their relation with the corporation on the one hand and on the other hand they must specify concrete objectives regarding the composition of the board taking into account the international activities of the company, the potential conflict of interest, an age limit and diversity[71].

The members of the Supervisory Board must be elected on individual bases[72] and one provision states also some limitations: the Board should have an adequate number of independent members that have no prior contact with the company and a maximum of two former members of the Management Board can be a part of the Supervisory Board[73]. By this provision, in my opinion, the legislator makes sure that the Management is not perpetuated in the Supervisory Board and that there are independent members that come with knowledge from outside of the system in which the business operates. For the German companies, the international board members that are elected in the Supervisory Board are few, only 7 percent of board members are international board members, compared to the United States which have 31 percent and Switzerland that has 45 percent[74].

Every member of the Supervisory Board must make sure that he has sufficient time to perform his duties towards the company, and if the member of the Supervisory Board comes

[69] *Id.* Art 5.4.1.
[70] *Id.* Art 5.1.2.
[71] *Id.* Art 5.4.1.
[72] *Id.* Art 5.4.3.
[73] *Id.* Art 5.4.2.
[74] INSTITUTE OF DIRECTORS, *supra* note 36, at 200.

from a Management Board of a different company he is not allowed to accept more than three Supervisory Board mandates[75]; with this provision the legislator ensures that the members will have the necessary time to fulfill their duties.

There are two very interesting provision in this article, one that states that the Supervisory Board members should form committees that should have sufficient expertise for the specific tasks they have to fulfill (an Audit Committee)[76] and another one that states that in order to nominate the shareholders representatives in the Supervisory Board there should be a nomination committee[77]. It is not uncommon to find representatives of banks in the Supervisory Boards of companies. There is a lot of discussions among the practitioners about the board composition because in some cases you could have members that have no idea about the business that they are supervising.

The compensation offered to the members of the Supervisory Board is decided by a resolution of the General Meeting or in the Articles of Association. The amount that will be received should take into account their tasks and the financial state of the company. Like the compensation received by the Management Board, their compensation has to be reported in the Management Report so that everybody interested can see it[78].

Supervisory Board Members have to act in the best interest of the company, they are not allowed to take advantage of the business opportunities that might occur and they can't pursue their personal interest. If there is such a conflict of interest, the member should inform the Supervisory Board and if the conflict of interest is material or it is not temporary it could

[75] German Corporate Governance Code, *supra* note 40 Art 5.4.5.
[76] *Id.* Art 5.3.2.
[77] *Id.* Art 5.3.3.
[78] *Id.* Art 5.4.6.

cause a termination of his mandate[79]. This provision insures that the business can protect itself against board members that could take decisions detrimental to the company.

The last provision of this article states that the Board must examine the efficiency of its activities on a regular basis[80], but this in my opinion is a subjective analysis because they will never have a bad review of their own work.

In Germany there is a practice that the former CEO will become the chairman of the Supervisory Board[81]. As pointed out by some authors, this is not the best solution because a CEO is a dynamic individual that deals with everyday life of the business and it could be impossible to transform in a non-executive chairman with a truly independent mind[82]. It is my opinion that the former CEO, if he was to be elected a member of the Board he should not be chairman during the first years, I would say at least five because as we know in real life it is very hard to have a radical change in thinking and acting.

2.2.5 Transparency

The company has to treat all shareholders equally and they have to be informed every time something important happens in the company's life. Also, the company has to disclose all important information including annual reports, financial reports and the date for the general meeting in advance so that the shareholders can participate[83]. With regards to the disclosure obligation, the information that has to be disclosed outside of Germany must be disclosed within Germany, so that the ones that have a legitimate interest will know what is happening[84]. This is in my opinion a very interesting provision, because the law applies extraterritorial and even though the legal provisions don't exist in Germany, if the company

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[79] *Id.* Art 5.5.
[80] *Id.* Art 5.6.
[81] INSTITUTE OF DIRECTORS, *supra* note 36, at 200.
[82] *Id.* at 219.
[83] German Corporate Governance Code, *supra* note 40 Art 6.
[84] *Id.* Art 6.2.

has to disclose some information under United States law, they also have to disclose it in Germany.

2.2.6 Reporting and Audit of the Annual

Shareholders and other interested parties are informed about the financial health of the company by Management Board after they have been examined by the Supervisory board and by an auditor. The legal documents that are used to inform the shareholders are called Consolidated Financial Statements and the Group Management Report[85].

The Management Board has to prepare the Annual Financial Statements, the Consolidated Financial Statements, and the Compensation report that must contain also a Corporate Governance Report in which the company discloses any information on stock options programs and similar securities-based incentive systems of the company[86].

There is an interesting provision in this article that requires the company to publish a list of third party companies in which it owns stocks that are not of minor importance for the company. The company has to provide among others the amount of the shareholding and the name of the company in which they own the shares[87]. This is a good way for the shareholders to know how the money is spent and what are the investments done in order to improve the company's financial life.

The Supervisory board commissions the auditor to conclude the audit[88]. After the auditor has been elected and the audit has started he has disclosed any information that might be detrimental to the company.

[85] *Id.* Art 7.
[86] *Id.* Art 7.1.2.
[87] *Id.* Art 7.1.4.
[88] *Id.* Art 7.2.2.

The auditor has to report on any facts or events that are important for the Supervisory board and the Management board that arise during the audit[89].

It is very important to have a complete disclosure with regards to the reporting and the auditing of the company and it is important to point out that in Germany they use the true and fair view principle in accounting, that shows the actual condition of financial and earning situation of the company[90]. In order for the audit to have any value, the accounting standards and measures must always be made transparent so they could be easily understood by average experts, because as we have seen in the Enron case that was discussed in the beginning of the paper, accounting is not an exact science, it can be easily manipulated and when the real financial situation will unfold it could be a disaster for the company.

The GCGC uses recommendations and suggestions. The recommendations are marked by the word shall, by using this phrasing the companies can go around them but then they are obligated to explain why. The suggestions are identifiable by the word should, and by this wording the companies can go around those provision without having to explain why[91].

2.3 Codetermination

Codetermination is a concept that allows workers to be elected in the supervisory board of the German companies. This concept is called by some authors the "German problem" because of the board size, their independence and the international composition of the board affects the "checks and balances" solution between the executives and the supervisors of the German two-tier system[92].

[89] *Id.* Art 7.2.3.
[90] Kort, *supra* note 37, at 6.
[91] German Corporate Governance Code, *supra* note 40 Art 1.
[92] INSTITUTE OF DIRECTORS, *supra* note 36, at 200.

There are currently three laws that address Codetermination in Germany[93]:

- The Montana Codetermination Act – this act was imposed to Germany after they lost the 2nd world war to hinder the weapon industry. It is applicable to companies with more than 1000 employees and provides equal representation for them in the Supervisory Board[94]
- The 1976 Codetermination Act – the company has to have at least 2000 employees and it provides equal representation for the employees in the Supervisory Board[95]
- The 2004 Third Part Act – it applies to companies that have various judicial forms, that have between 500 and 2000 employees, and this act gives one third of the supervisory board seats to the employees[96]

2.4 Societas Europeae

The European Company (SE) was made possible by an EU Council regulation in 2001, and it took almost 20 years for this regulation to exist. It is seen by some authors as an alternative to the German Board Structure[97].

As it can be seen in the Regulation[98] there is the possibility to choose between a one-tier board structure like the Anglo-Saxon system or a two-tier system like the German one. Because of this possibility there is a wide application of the two models within the European Union.

With regards to Germany, this was a compromise that they undertook because their law provides for codetermination and a lot of foreign investors didn't want to incorporate in

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[93] Zenovia Cristiana Pop & others, *A Comparative Study of Corporate Governance Issues: The Case of Germany and Romania.*, 11 IUP JOURNAL OF CORPORATE GOVERNANCE 4,5 (2012).
[94] *Id.* at 4.
[95] *Id.*
[96] *Id.* at 5.
[97] INSTITUTE OF DIRECTORS, *supra* note 36, at 195.
[98] Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European Company (SE) art 38.

Germany because of this provision. As it can be seen in the Regulation that was mentioned earlier there is a freedom to choose the individual shapes of the codetermination system and the management has to discuss this with the employees.

As was shown by the ECJ in the Centros[99] case, there is a freedom of establishment in the EU, so there were ways to circumvent the codetermination requirement and the two-tier system, so the Regulation in my opinion only states the obvious , that you are allowed to choose how to govern your company and what model to apply.

2.5 Mannesmann Case

This was a German landmark case that was decided by the Highest German Court and it brought new questions regarding the payment of the board members[100].

In the year 2000, Mannesmann, a German telecommunication company, was taken over by another competing company called Vodafone. At that time, this takeover, was one of the biggest mergers and acquisitions deals in the world, worth almost 200 billion Euros in today's money[101].

Mannesmann was an old company that was founded as a tube manufacturer company, that later diversified its activity and going into the telecommunication industry. During the 1990 until the year 2000 there were a lot of takeovers taking place in the world, that is why most of the legislation regarding corporate governance was enacted starting from the year 2000. In this case, the company had many shareholders that individually owned small portions of the company shares; this is in my opinion one of the reasons why the takeover was possible. In the beginning Mannesmann wanted to acquire Orange another telecommunication company, so they were playing the same game as Vodafone. When the bid was launched, Mannesmann

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[99] Centros Ltd v Erhvervs- og Selskabsstyrelsen (1999) C-212/97 (European Union|EU.INT European Court of Justice).
[100] Kort, *supra* note 37, at 30.
[101] *Id.* at 31.

tried to resist and there were a lot of commercial ads made by each company to encourage and discourage the takeover, but eventually the majority of the shareholders decided to sell.

For the purpose of this paper, the interesting fact is that some of the management and supervisory board members were accused of giving bribe to other in order for the takeover to happen. The German court that decided the case used the waste of corporate assets doctrine, and stated that good Corporate Governance requires that appreciation awards should be agreed upon in advance, when signing the employment contract[102].

In my opinion this case clearly shows the conflict of interests that is why on the one hand conflict of interest is regulated now in the GCGC and on the other hand remuneration is also regulated and has to be decided transparent by the interested parties.

Chapter 3 - Corporate Governance Rules in Romania

3.1 History of Corporate Governance in Romania

Unlike Germany and other western countries, when World War II ended, Romania's political system transformed into a communist one. This is particularly interesting for our analysis because under the communists every business was stated-owned. After the Romanian revolution of 1989, the communist regime fell and democracy was born. Because of the political context that existed during the 1990, Romania started a long process to enter the EU, a process that ended seventeen years later, in 2007 when Romania became a member of the EU.

In order for Romania to become a member of the EU, the state-owned companies had to be privatized and another long process was started. The privatization process was important because, on the one hand, a key principle in the EU is a free market economy with minimal

[102] *Id.*

state intervention and, on the other hand, the economic giants were underperforming, they created huge debts and the companies were highly influenced by the political color of each party that came after the communists. Unfortunately, the privatization process is still a problem in Romania[103] and in my opinion, because of the fact that Romania didn't have a corporate governance rules it was possible for external investors to purchase flourishing companies and destroy them in order to eliminate competition in the international markets. I will discuss later in the paper the still existing state-owned enterprise's problem.

The rules for Corporate Governance were implemented in Romania because, on the one hand, the privatization process required an improvement in the management process and, on the other hand, the control and supervision had to be shifted from the political organization to the Board of Directors that existed in every company[104].

3.2 Corporate Governance Rules in Germany

The rules for corporate governance can be found in various laws[105]:

- The Company Law (Legea societăților Comerciale)
- The Commercial Code (Codul comercial)
- The Law on the capital market with all its amendments (Legea Pieței de Capital actualizată)
- The Law regarding the Insolvecy Proceedings (Legea privind procedurile de Insolvență)
- The Law on Accounting with all its amendments (Legea Contabilității actualizată)
- The Law on Privatization (Legea privind Privatizarea)
- The Labour Code (Codul muncii)

[103] FELEAGĂ et al., *supra* note 3, at 4.
[104] Grosu Maria, *Codes and Practices of Implementation of Corporate Governance in Romania and Results Reporting*, 1 ANNALS OF FACULTY OF ECONOMICS 251, 2 (2011).
[105] FELEAGĂ et al., *supra* note 3, at 4.

- The Law on the collective employment contract (Legea privind contractual individual de muncă)
- Specific regulations on the harmonization of the Romanian accounting system with the European Directives and International Accounting Standards
- Regulations issued by the Romanian National Bank and the Securities Commission
- Government Emergency Ordinance number 109/2011 on Corporate Governance that deals with the companies that are owned by Romanian state or the ones in which the state has participative rights (stock, shares, etc) – (Ordonanța de Urgență a Guvernului Numărul 109/2011 privind Guvernanța Corporativă a Întreprinderilor Publice)

Until 2001 there was no Corporate Governance Code, and the OECD made a recommendation to Romania to have a strong private sector with an effective ownership control structure and the first step was done by the Bucharest Stock Exchange that adopted the Romanian Corporate Governance Code in 2001[106]. Romania was one of the first Eastern European Country to adopt a Corporate Governance Code[107].

The first Code adopted by the Bucharest Stock Exchange introduced a virtual tier called the „plus tier" which meant that the companies listed in that tier had an additional layer of transparency[108]. The first version was not successful because, on the one hand, there was only a company that entered in that tier[109] and, on the other hand, the implementation of the Code had some fundamental flaws and inconsistencies[110]:

- The relationship between shareholders and managers lacked a precise analysis

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[106] Ionel-Alin Ienciu, *The Relationship between Environmental Reporting and Corporate Governance Characteristics of Romanian Listed Entities*, 11 JOURNAL OF ACCOUNTING AND MANAGEMENT INFORMATION SYSTEMS 267, 4 (2012).
[107] Sorana Mihaela MĂNOIU, *Analiză Conceptuală a Codurilor de Guvernanţă Corporativă Din România, Ungaria Şi Bulgaria: Responsabilitate Sau Antreprenoriat?*, 12 AUDIT FINANCIAR 3 (2014).
[108] FELEAGĂ et al., *supra* note 3, at 6.
[109] *Id.* at 4.
[110] *Id.*

- The stakeholders were rarely involved in the decision making process
- There was no conceptual framework for an efficient market
- The international accounting system had failed to be implemented
- The financial statements of the companies had a poor control mechanism to show a fair and relevant disclosure

In the year 2004, the World bank published a report, that measured the implementation of the Corporate Governance Code and recommended a new Corporate Governance Code to be drafted that should protect shareholder rights, provide training to board members, revise the Company Law with emphasis on shareholder rights and on that of the board of directors, and create a Corporate Governance Institute[111]. This recommendations were done in order to help Romania with its process of EU accession. The Romanian policymakers complied and in 2003 the Institute of Corporate Governance of the Bucharest Stock Exchange was created[112].

In 2008 a new Corporate Governance Code was drafted by the Bucharest Stock Exchange that was more complex and more adapted to the European legislation. Publicly traded companies can adopt and comply to the Code only voluntarily, and I think the Romanian policy makers thought that the market will encourage companies to comply in order to attract foreign investors.

There is a lot of discussion this year, 2015, to adopt a new Corporate Governance Code that will replace the one from 2008 that is currently enforced. The new Code is a joint project of the Bucharest Stock Exchange and the European Bank for Reconstruction and Development to improve the local "corporate governance climate". In developing the new Corporate Governance Code, they will take into consideration the changes of the legal framework in

[111] Report on the observance of standards and codes (ROSC) , Corporate Governance Country Assessment, available at http://www.worldbank.org/ifa/rosc_cg_rom.pdf accessed on 26.03.2015.
[112] Ienciu, *supra* note 106, at 5.

Romania and the EU, the new aspirations of the society and of the parties involved in managing the business, the international standards and the experience gained from the first two Codes. The objectives of this project is to strengthen the monitoring and implementation of the new code and to enhance the key practices and their disclosure in Corporate Governance of the listed companies[113].

Ludwik Sobolewsi, the CEO of the Bucharest Stock Exchanges said in a press release that: This Code (the new one) will be in a way innovative, because it will not contain the classical issues which are normally treated when it comes to corporate governance. We have a chance to generate essential progress when having these pragmatic rules in the Corporate Governance set of provisions. That's why we decided to tackle, also, some issues which are not the classical topics touched by the, generically speaking, Codes of Corporate Governance. For instance, we will expect for listed companies that they will publish their dividend policies, to inform the investors what guidelines they give when it comes to this dividend policy, and what investors could expect.

For the purpose of this paper we will analyze and discuss the Bucharest Stock Exchange Corporate Governance Code[114] that entered into force in 2008 and is still enforced today.

The latest version of the Bucharest Stock Exchange Corporate Governance Code is divided in 11 articles that contain 19 principles and within those articles it contains 41 recommendations.

3.2.1 Corporate Governance Framework[115]

"Principle 1: The issuers will adopt a clear and transparent corporate governance framework, which shall be adequately disclosed to the general public."

[113] Consultations for the New Bucharest Stock Exchange Corporate Governance Code, available at http://www.bvb.ro/press/2014/press_release_consultations_on_Corporate_Governance_Code_22122014.pdf , accessed on 26.03.2015.
[114] Bucharest Stock Exchange Corporate Governance code from 2008 , available at http://www.ecgi.org/codes/documents/bucharest_se_code_jan2009_en.pdf , accessed on 22.03.2015
[115] Art. 1 of the Bucharest Stock Exchange Corporate Governance Code

Within this article there are also some recommendations that I would like to point out. The first one states that the issuers must have Corporate Governance Regulations that should describe the main aspects of the companies' corporate governance and the framework used should be defined in the previously stated Regulation[116]. It further states that the framework should describe the functions of the Board of Directors and the Management Board and also describes their powers and responsibilities[117]. The last recommendation made in this article refers to an annual report that issuers must adopt and disclose in which they have to describe the corporate governance events that took place in the preceding year. If an issuer chooses not to implement the recommendations of this Code, he must explain why in this report and also in the Comply or Explain statement[118].

As we can see from the wording of the text, the first article of the Code meets the requirements of the OECD and is to some extent similar to the German Code.

3.2.2 The Share & other financial instruments holders' rights[119]

"Principle 2: The issuers shall respect the rights of their share- and other financial instruments holders and ensure they receive equitable treatment".

"Principle 3: The issuers shall endeavor their best efforts to establish a policy of effective and active communication with their share-and other financial instruments holders."

The first of the recommendations in this article states that all the holders of financial instruments must be treated equitably and all financial instruments must carry the same rights; in case the issuer wants to change the rights offered to the holders, the affected holders must agree to that change by voting[120]. The recommendations further state that the issuer shall use

[116] Art. 1 Rec. 1 of the Bucharest Stock Exchange Corporate Governance Code
[117] Art. 1 Rec. 2 of the Bucharest Stock Exchange Corporate Governance Code.
[118] Art. 1 Rec. 3 of the Bucharest Stock Exchange Corporate Governance Code.
[119] Art. 2 of the Bucharest Stock Exchange Corporate Governance Code
[120] Art. 2 Rec. 4 of the Bucharest Stock Exchange Corporate Governance Code.

his best efforts to facilitate the participation of the shareholders in the General meeting and to facilitate the full exercise of their rights[121]. The issuer shall agree with the shareholders on the rules and procedures that must be followed to have an effective General meeting but they must respect the right of each shareholder to express his or her opinion on the matters that are being discussed[122]. The company should encourage the shareholders to take part in the General meeting that should encourage the dialog between the two and furthermore it must allow the vote of the shareholders that can't attend the meeting through a proxy[123]. In order for the issuer and the shareholder to have a better communication and easily access to relevant information in order for the later to exercise their rights, the former must have a specific section on their internet page; the relevant information should contain among others the exercise of the voting rights in the General meeting, the date for the meeting, the documents needed to understand the agenda, special proxies templates and the procedure for the access and participation in the General meeting[124].

This article presents similarities with the one in the German Corporate Governance Code and it complies with the OECD principles.

3.2.3 The role and duties of the Board[125]

"Principle 4: The issuers are governed by a Board of Directors that meets at regular intervals, and that adopts decisions, which enable it to perform its functions in an effective and efficient manner."

"Principle 5: The board of an issuer will be responsible for its management. It will act to the best interests of the company and will protect the general interests of the shareholders by

[121] Art. 2 Rec. 5 of the Bucharest Stock Exchange Corporate Governance Code.
[122] Art. 2 Rec. 6 of the Bucharest Stock Exchange Corporate Governance Code.
[123] Art. 2 Rec. 7 of the Bucharest Stock Exchange Corporate Governance Code.
[124] Art. 2 Rec. 8 of the Bucharest Stock Exchange Corporate Governance Code.
[125] Art. 3 of the Bucharest Stock Exchange Corporate Governance Code

ensuring the sustainable development of the company. It will function in a well-informed manner as a collective body."

The recommendations made in this article start by stating that the board should meet as often as it is necessary to fulfill their obligation towards the company and the first recommendation also states that it would be appropriate for the board to meet at least once every 3 months[126]. Further, the recommendations state that the board should adopt rules in order to prevent insider dealing and market manipulation of its securities made by its members or the employees of the company[127]; the board should also adopt rules on notification about trading of shares or other financial instruments by directors and this rules should specify which information about this transactions should be disclosed to the general public or the market[128].

In this article, the recommendations also establish a set of tasks to be fulfilled by the Board of Directors, tasks that are not exhaustive: they must examine and approve the financial, operational and strategic plans of the company; they must evaluate the adequacy of the administrative, accounting and organizational structure of the issuer and the general performance of the company; they must examine and approve in advance transactions that could have an important impact on the company's profitability, liabilities, assets and financial position; they should evaluate once a year the composition and performance of the Board of Directors and its committees and they must provide information related to the implementation of the Code in the Chapter on Corporate Governance in the issuers annual report[129].

This article is consistent with the OECD principles, and it is similar to the articles from the German Corporate Governance Code, but one of the big differences is that by German

[126] Art. 3 Rec. 10 of the Bucharest Stock Exchange Corporate Governance Code.
[127] Art. 3 Rec. 11 of the Bucharest Stock Exchange Corporate Governance Code.
[128] Art. 3 Rec. 12 of the Bucharest Stock Exchange Corporate Governance Code.
[129] Art. 3 Rec. 13 of the Bucharest Stock Exchange Corporate Governance Code.

Company law, for the big listed corporations, it is mandatory to have a two tier system, while in Romania this is not a mandatory requirement.

3.2.4 Composition of the Board[130]

"Principle 6: Without any prejudice to the principles of the Board decision-making process, the composition of an issuer's board should ensure a balance of executive and non-executive directors) and in particular independent non-executive directors) insofar that no individual or small group of individuals can dominate the board's decision taking"

> Principle 7: An adequate number of non-executive directors shall be independent, in the sense that they do not maintain, nor have recently maintained, directly or indirectly, any business relationships with the issuer or persons linked to the issuer, of such a significance as to influence their autonomous judgement. Renunciation to a term, by an independent director, shall be accompanied by an extensive, detailed statement regarding the reasons for such action.

"Principle 8: The Board has a number of members that warrants and effective capacity to supervise, scrutinize and evaluate the activity of the executive directors and the fair treatment of all the shareholders."

The recommendations start by stating that the Board should be composed of members that will allow it to take decisions of which they are fully aware, because they are liable for those decisions taken for the company[131]. Further it is stated that consultative committees should be set up to examine specifics and advise the board about them[132]. Within the recommendations it is stated that the Board of Directors shall evaluate on specific criteria the independence of

[130] Art. 4 of the Bucharest Stock Exchange Corporate Governance Code
[131] Art. 4 Rec. 14 of the Bucharest Stock Exchange Corporate Governance Code.
[132] Art. 4 Rec. 15 of the Bucharest Stock Exchange Corporate Governance Code

its non-executive members[133]. The final recommendation made in this article states that the members of the Board should improve their knowledge and update their skills in running the company and also they should improve their knowledge in Corporate Governance best practices to be able to fulfill their roles in the Board or in the committees established by the Board[134].

This article is to some extent similar to the ones in the German Corporate Governance Code, but there are differences in the composition of the Board, because for example in Germany half of the Board of Directors must be composed of workers and employees representatives, while in Romania there is no such requirement. The OECD does not make any references for the composition of the Board.

3.2.5 Appointment of Directors[135]

"Principle 9: The appointment of Directors should be a formal, rigorous and transparent procedure. Such procedure shall use objective criteria and ensure timely adequate information on the personal and professional qualifications of the candidates. The cumulative voting shall constitute an adequate procedure for the appointment of Directors."

"Principle 10: The Board of Directors shall evaluate whether to establish among its members a nomination committee made up, mainly of independent directors."

The first recommendation from this article states that every candidate for a director seat must disclose information on his qualifications, his traits and an indication if he is eligible to be appointed as independent director and the disclosure will be published on the company's internet site[136]. The last recommendations state that, in case a nomination committee is established, they must make recommendations to the board for the future members. In order

[133] Art. 4 Rec. 16 of the Bucharest Stock Exchange Corporate Governance Code.
[134] Art. 4 Rec. 17 of the Bucharest Stock Exchange Corporate Governance Code.
[135] Art. 5 of the Bucharest Stock Exchange Corporate Governance Code
[136]Art. 5 Rec. 18 of the Bucharest Stock Exchange Corporate Governance Code.

for the nomination committee to make a recommendation they must evaluate the future members based on their skills, knowledge and their experience[137].

This article and the one in the German Corporate Governance code are similar, but we have to keep in mind the German Co-determination law. With regards to the OECD principles, this article makes sense because I could not imagine how a company that appoints directors without having a transparent, rigorous and formal procedure of appoint directors would work in the modern day economic life.

3.2.6 Remuneration of Directors[138]

"Principle 11: The company will secure the services of good quality directors and executive managers by means of a suitable remuneration policy that is compatible with the long-term interests of the company"

In my opinion, the most important recommendation from this article is the one that states the obligation of the company to disclose its remuneration policy in the Corporate Governance Regulation, the amount should be disclosed in the annual report with a distinction being made between the fixed and the variable components of this remuneration[139]. In order to have a valid remuneration policy, a remuneration committee should be established by the Board[140]. The remuneration committee members should have a sufficient number of independent directors and it should be made up exclusively from non-executive directors[141]. The remuneration committee should make proposal on the remuneration of the members to the board[142].

[137] Art. 5 Rec. 20 of the Bucharest Stock Exchange Corporate Governance Code.
[138] Art. 6 of the Bucharest Stock Exchange Corporate Governance Code
[139] Art. 6 Rec. 24 of the Bucharest Stock Exchange Corporate Governance Code.
[140] Art. 6 Rec. 21 of the Bucharest Stock Exchange Corporate Governance Code.
[141] Art. 6 Rec. 22 of the Bucharest Stock Exchange Corporate Governance Code.
[142] Art. 6 Rec. 23 of the Bucharest Stock Exchange Corporate Governance Code.

The German Code on Corporate Governance and the Romanian one, contain provisions regarding the remuneration of directors. In Germany, the compensation is specified by resolution of the General Meeting or in the Articles of Association. In Romania, in my opinion, the Board can do whatever they want with regards to their salaries.

3.2.7 Transparency, Financial Reporting, Internal Control and Risk Management[143]

"Principle 12: The corporate governance framework must ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership and governance of the company".

"Principle 13: The board will establish strict rules, designed to protect the company's interests, in the areas of financial reporting, internal control and risk management."

The first recommendation from this article states that in accordance with the high quality standards of accounting and financial and nonfinancial disclosure the issuer has to prepare and disseminate relevant and continuous information; the disclosure has to be written in Romanian and in English language[144]. Further, the recommendations state that in order to provide relevant analysis for the investors, the issuer has to organize a meeting at least once a year with analysts, brokers, rating agencies and other market experts[145].

Another interesting recommendation states that the Board should chose some of its members for an auditing committee in order to help with the financial reporting, internal control and risk management. Before this committee is set up, the Board should cooperate with the internal and external auditor; afterwards the Board should meet with the auditors at least twice per year to discuss issues related to financial reporting, internal control and risk

[143] Art. 7 of the Bucharest Stock Exchange Corporate Governance Code
[144] Art. 7 Rec. 25 of the Bucharest Stock Exchange Corporate Governance Code.
[145] Art. 7 Rec. 26 of the Bucharest Stock Exchange Corporate Governance Code.

management[146]. The audit committee should be composed exclusively out of non-executive directors containing a sufficient number of independent directors[147], and the committee should examine the effectiveness of the financial report, the internal control and the risk management[148]. The committee should meet as much as it is necessary to complete their job, but at least twice a year[149]. Furthermore it is stated that the committee should assist the board in supervising the fairness of the financial information provided by the company, and in particular they should assist the Board by checking the compliance with the accounting standards used by the company[150]. In case the company uses an external auditor, the audit committee is the one that makes recommendations to the Board about the appointment, remuneration and removal of the external auditor[151].

This article presents some similarities with the articles from the German Corporate Governance Code and the OECD principles. There is also a big difference, in Germany it is mandatory to use an external auditor. In my opinion, the German code is more precise about the rules that should be used. The article from the Romanian Code has an interesting provision stating that the information should be disclosed also in the English language, but the legislator failed to provide precise rules about who does what and how.

3.2.8 Conflict of interests and related parties transactions[152]

"Principle 14: The Board of Directors shall adopt operating solutions suitable to facilitate the identification and an adequate handling of those situations in which a director is bearer of an interest on his/her behalf or on behalf of third parties."

[146] Art. 7 Rec. 27 of the Bucharest Stock Exchange Corporate Governance Code.
[147] Art. 7 Rec. 29 of the Bucharest Stock Exchange Corporate Governance Code.
[148] Art. 7 Rec. 28 of the Bucharest Stock Exchange Corporate Governance Code.
[149] Art. 7 Rec. 30 of the Bucharest Stock Exchange Corporate Governance Code.
[150] Art. 7 Rec. 31 of the Bucharest Stock Exchange Corporate Governance Code.
[151] Art. 7 Rec. 32 of the Bucharest Stock Exchange Corporate Governance Code.
[152] Art. 8 of the Bucharest Stock Exchange Corporate Governance Code.

“Principle 15: The directors will take decisions in the interests of the company and will refrain from taking part in any deliberation or decision that creates a conflict between their personal interests and those of the company or any subsidiary controlled by the company.”

“Principle 16: The Board of Directors shall, after consulting with the internal control body, establish approval and implementation procedures for the transactions carried out by the issuer, or its subsidiaries, with related parties.”

It is stated is the recommendations from this article that directors should avoid a direct or indirect conflict of interest and in case this happens the member should inform the Board if such conflicts appear[153].

With regards to related parties transaction, the Board should establish a fair procedure following some specific criteria like asking an independent expert, the use of a prior opinion of the internal control body and the use of an independent director that have no conflict of interest[154]. The procedure should define which transactions need their approval[155].

This article complies with the OECD principles, but if we compare it to the German Corporate Governance Code we see that to some extent they present similarities but in the Romanian code there is no sanction for a member that has a conflict of interest while in the German Code it is written in black and white, namely as we see in art 5.5.3 of the German Corporate Governance Code, a conflict of interest can lead to the termination of a members mandate.

[153] Art. 8 Rec. 33 of the Bucharest Stock Exchange Corporate Governance Code.
[154] Art. 8 Rec. 34 of the Bucharest Stock Exchange Corporate Governance Code.
[155] Art. 8 Rec. 35 of the Bucharest Stock Exchange Corporate Governance Code.

3.2.9 Treatment of Corporate Information[156]

"Principle 17: Directors and managers shall keep confidential the documents and information acquired in the performance of their duties and shall comply with the procedure adopted by the issuer for the internal handling and disclosure to third parties of such documents and information".

This article has only one recommendation in which it is stated that the managers should act in a correct manner and handle the information in a correct way. The managers should make a proposal to the Board of Directors to adopt an internal procedure to handle and disclose information concerning the business to third parties, with particular attention to price sensitive information[157].

This article is similar to the article in the German Corporate Governance Code, but there it is addressed in the part that deals with conflict of interests. The OECD makes no direct mention about corporate information but it implies it.

3.2.10 Corporate Social Responsibility[158]

"The corporate governance framework must know and recognize the legally established rights of stakeholders and encourage active cooperation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises."

Because of the Romanian communist history, the first recommendation requires that the issuer should pay special attention to the environment and put its best efforts to integrate economic and social concerns[159]. The second recommendation requires the issuer to enhance the role of the employees in the company and to encourage trade unions. The issuer should

[156] Art. 9 of the Bucharest Stock Exchange Corporate Governance Code
[157] Art. 9 Rec. 36 of the Bucharest Stock Exchange Corporate Governance Code.
[158] Art. 10 of the Bucharest Stock Exchange Corporate Governance Code.
[159] Art. 10 Rec. 37 of the Bucharest Stock Exchange Corporate Governance Code.

develop and implement the Corporate social responsibility practices with the help of employees, trade unions, creditors, consumer and investors[160].

This article takes into consideration the OECD principles and it is similar to what is implied by the German Corporate Governance Code.

3.2.11 Management and Control Systems[161]

"Principle 19: When a two-tier management and control system is adopted, the above articles shall apply insofar as compatible, adapting individual provisions to the two-tier system, consistently with the objectives of good corporate governance, transparency of information and protection of investors and the markets, pursued by the Code in conformity with this article."

In my opinion this principle was introduced, because of the German economic dominance in the European Union and the world. The first recommendation requires the Board to inform the shareholders and the market when a new management and control system is proposed[162]. The second one requires the issuer to explain in the chapter dedicated to corporate governance, how the Corporate Governance Code applies to the system that was introduced[163]. The last recommendation adapts the Code to the German Corporate Governance code and describes which provision can be applied for the two Boards that exist in the German legislation, the Management Board and the Supervisory Board (Board of Director in the Romanian)[164].

In my opinion, this article was introduced in order for the Romanian companies that use the two tier system to be able to comply with the code; the article is not contrary to the OECD principles.

[160] Art. 10 Rec. 38 of the Bucharest Stock Exchange Corporate Governance Code.
[161] Art. 11 of the Bucharest Stock Exchange Corporate Governance Code
[162] Art. 11 Rec. 39 of the Bucharest Stock Exchange Corporate Governance Code.
[163] Art. 11 Rec. 40 of the Bucharest Stock Exchange Corporate Governance Code.
[164] Art. 11 Rec. 41 of the Bucharest Stock Exchange Corporate Governance Code.

3.3 Corporate Governance in State owned enterprises

In developing economies, like in the case of Romania, a large number of big companies are state-owned. The companies are usually economic giants that are of crucial importance to the economy and to the development of the country, like energy companies, transport, telecommunication, gas and others.

Because of the fact that the economy is developing, state-owned companies should be a good example for corporate governance and responsibility.

In state-owned companies, the shareholder is the Government through a Minister. In the case of Romania, the companies are divided into autonomous government-owned and joint-stock having the state as the only shareholder, or after the privatization process occurred, the state is the controlling shareholder[165].

The members of OECD own on average 50 enterprises that are owned by the state as a single shareholder or as a majority one. As was previously stated in this paper, Romania is not a member of the OECD and has 720 state-owned enterprises and it is only surpassed by Poland and the Czech Republic that have around 1000 each and of course by China that has around 17000[166].

The Romanian policy makers intervened and issued the Emergency Government Ordinance, nr. 109 from 2011 to regulate the Corporate Governance of state-owned enterprises. This piece of legislation complies with the OECD guidelines recommendations on state-owned Enterprises and it also complies with the structure of the corporate governance system provided by the Romanian company law.

[165] Mihaela DUMITRAŞCU et al., *The Practical Implementation of Corporate Governance Principles for Romanian State Owned Enterprises.*, 13 AUDIT FINANCIAR (2015).
[166] *Id.* at 4.

The Ordinance 109/2011 represents a genuine reform and the cornerstone consists in limiting the public authority to interfere in the management of the companies and in the de-politicization of the Board of Directors and executive managers[167].

Like any piece of legislation issued in Romania, this Ordinance was analyzed by professionals and highly criticized because, on the one hand, it totally disregarded the stakeholders and, on the other hand, it discarded the social and environmental responsibility for this company's[168]. Another criticism was brought because the Ordinance does not refer to the Corporate Governance Codes, the Codes of best practices or other soft laws[169].

In my opinion, the Romanian policymakers tried to regulate an area that they don't clearly understand. This Ordinance brought some changes, like foreign managers for the state-owned enterprises, but even so the companies still have loses and can't compete with their international rivals[170]. Every privatization that was done by the state was accompanied by at least one scandal that involved bribes.

With regards to legislation, until there will be a clear separation of the three functions the state plays as a shareholder: owner, regulator and industrial policy maker[171], Corporate Governance in Romania will still be a taboo subject.

3.4 Oltchim case[172]

Oltchim, formerly called Govora Chemical Plant, was established during the communist regime, in the 1970. It was set up to function as a chemical plant to help another company to refine oil. The company was an economic giant and it even had a subsidiary in Germany, Oltchim GmbH.

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167 Radu N. Catană, *Shortcomings of The Recent Reform of State-Owned Enterprises" Corporate Governance in Romania*, 51 CURENTUL JURIDIC 118, 2 (2012).
168 *Id.*
169 Catană, *supra* note 167.
170 Tarom, the national airline is the first company to have a foreign manager.
171 Catană, *supra* note 167, at 3.
172 Kort, *supra* note 37, at 5.

The problems started to unfold after the primary plant was shut down by the Government in 2010. In 2011, the company got a fine of 14,3 million euros for environmental pollution. Today the company is insolvent, has a debt of about 700 million euros and the Government tried to privatize it.

In my opinion Oltchim disregarded any recommendations and codes for Corporate Governance. The former CEO of the company was in the same position for 21 years, the longest period for any CEO from Romania. When the state agencies came and checked the books, they found that he used the company's money for personal interest and he had large incomes and benefits for Romania, like an average 50.000 Euros monthly salary and exclusive vacations paid by the company.

In 2012, the former CEO and his team resigned collectively and the government appointed interim directors on a political bases only without consulting the minority shareholders. The resignation is thought to have come after the enforcement of the Emergency Government Ordinance 109/2011.

The Government tried to privatize the company in which it held a 54.8% share, but after a big scandal that is typical in the Romanian system, it failed to do so. The state is the majority shareholder in this company, and in my opinion they tried to apply the Japanese Corporate Governance model that I described in the first chapter of the thesis. In Romania, Corporate Governance was developed only recently, so they had the benefit to derive the Corporate Governance rules from every other Corporate Governance Code that was available. With regards to Oltchim, the model was applied in a bad way, and the state intervention in the strategic planning of the company was a disaster that ultimately brought the company in its current insolvent case.

In my opinion this case shows, on the one hand, that corporate governance was totally disregarded, and on the other hand, it shows that the privatization process that was undertook by the State was not efficient.

Conclusions

In order to have a working economy that focuses on the greater good and on social responsibility we need corporations that must apply Corporate Governance Rules. The Rules were established after big economic failures of large corporations and even though there are guidelines on Corporate Governance, like the OECD Corporate Governance Principles, they are not applied by corporations. Because the Corporate Governance Rules are not mandatory, the legislators from around the world assumed that the need for international investors will force companies to adopt the Corporate Governance Codes that are available in developed economies and there is no need for a mandatory legislation.

There are several models of Corporate Governance in the World, but for the purpose of this paper I only chose three, the American, the Japanese and the German. This models are in my opinion the leading ones and each of them has advantages and disadvantages.

The German legislator responded to a market reality, the need for foreign investors, so they adopted the German Corporate Governance Code. The code tries to set some rules that the corporations should follow that would determine the foreign investors to put their money in the corporations that comply with the rules.

The German Corporate Governance model uses a mandatory two-tier system for managing the company and one of the benefits of this system is that decisions are filtered and shareholders are better protected.

There are some disadvantages, one of which is the fact that the Code is not an act of the Parliament or a binding agreement between parties so there are constitutionality concerns and the rules not statutory law; the other one is the composition and size of the Supervisory Board because it can have 20 members from which half are theoretically qualified for the job because of the Codetermination Act and the other half are mainly representatives of banks and other members that might lack the particular knowledge of the business that they supervise.

Romania has been a democratic state for the last 25 years, and has been a member of the European Union for the last 8 years, so normally one would expect that it has a Corporate Governance Code that is issued by a legislative body, but this is not the case. As incredible as it may be, the only Corporate Governance Rules that exist in Romania are the ones issued by the Bucharest Stock Exchange. This code was issued in order for Romania's accession to the European Union, otherwise not even this Code would exist.

The Bucharest Stock Exchange Code was derived from the German one, but there are also differences that I pointed out in this paper, one of the most important one is that in Germany it is mandatory to have a two-tier system for the listed German stock corporation while in Romania there is no such rule. One of the most important similarity is that both of the Codes use recommendations and suggestions, the German Code states that explicitly within the first article by using the word shall for recommendations and should for suggestions, the Romanian Code issued by the Bucharest Stock Exchange uses principles that are suggestions and recommendations.

The Romanian Corporate Governance Code and the German Corporate Governance Code follow the OECD principles, but both of the codes have additional provisions that don't conflict with them.

In Romania, in my opinion Corporate Governance is a taboo subject. The Romanian companies won't comply with code because there are investors that are not concerned about their compliance with the code. It is my opinion that the Romanian legislator doesn't understand among others the difference between Director and Manager, they think that manager is the English word for Director (it is spelled the same in the Romanian language) so they have no idea what model to implement, a two-tier or one-tier. Even if a company would want to comply with the code and start researching the Romanian literature, the first Code that one finds is the one from 2001 that was changed; the 2008 Code that is enforced today, is not even available on the Bucharest Stock Exchange web page. For the purpose of this paper, I found the code on The European Corporate Governance Institute website.

As a recommendation, there is the need to have a Corporate Governance Code issued by the legislator in Romania that regulate Corporations behavior and management, otherwise the Romanian economic system will never fully developed and the Oltchim case that I presented might repeat itself in every publicly owned company.

If I had a company, I would definitely use a two-tier model to manage my company and I would adhere to the German Corporate Governance Code with some changes in the composition and numbers of the Supervisory Board.

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