Corporate governance in a radically changed world
a fresh look at the Rhineland model

The Anglo American system of corporate governance fails us all

The corporate governance issues which explain the collapse of the global financial system is a reminder that the power to make bad decisions in the interest only of personal greed can no longer be tolerated in progressive democracies. The financial collapse has in turn caused a sharp decline in global output. It is only now slowly recovering.[1] World stock markets in March 2010 show an astounding $20tr loss in value since December highs of some $61tr in 2007.[2] OECD growth, whilst recovering, is lacklustre.[3] Recent data on the US may herald a slide back into recession.[4] The *Made in America* financial crisis and the Anglo American model of corporate governance is, rightly, in the dog house - where it belongs.
As stock market data confirms, beyond a shadow of doubt, the Anglo American model has spectacularly failed to protect shareholder wealth - its professed primary intention[5]. Workers' capital[6] has been squandered on an epic scale. At the same time the prosperity of many millions of ordinary people has worsened. The sense of public outrage is understandable. Yet despite all the hype and the promises by politicians and policy makers that *things will be changed* – things, far from changing are returning to *business as usual*. The bankers are back in the saddle. Generous bonuses are being paid. The boards of many bank and non bank corporations alike in Anglo American jurisdictions have learnt little from the damage that has been inflicted. The folly of the business elites is being paid for by working people.

If politicians won't act then global trade unions must press resolutely for change. Bank and non bank corporations alike have to be properly, effectively and transparently supervised. Drawing strength from the excellent co-determination habits of Rhineland democracies[7] we have to challenge the autocratic, non-inclusive style of Anglo American unitary board governance arrangements - wherever they exist. To drive home the argument trade unions need to be able to prove that independently supervised corporations are better at protecting both worker prosperity, as well as shareholder value.

The voice of working people has to be taken into account in the supervision of the world's largest corporations. Democratic self-determination at the work place demands no less. This is the only way that the wrecking instincts of personal greed can be controlled. The well rehearsed argument that independent supervision will stifle innovation is self serving

[1] According to the latest IMF Outlook, renewed turbulence in financial markets—reflecting a drop in confidence about fiscal sustainability, policy responses, and future growth prospects—has cast a cloud over the outlook with renewed fears that weak employment numbers may cause the US to enter a fresh recession – a fea that has prompted further Quantitative Easing by the Federal Reserve.
[2] Source World Federation of Exchanges March 2010. Exchange values are around 40% below their 2007 highs, a loss of $20tr.
[3] For 2011, growth in advanced economies is expected to remain broadly unchanged at 2.5% from the April 2010 forecasts according to the IMF WEO (World Economic Outlook).
[4] As indicated by recent US tepid retail sales, rising unemployment and weak new home sales..
[5] Under Anglo American corporate law directors are portrayed as having a first duty to protect shareholder value.
[6] A reference to the pension funds of working people that are invested by institutional investors into stock markets.
[7] A reference notably to Germany and other democracies that border the River Rhine.

propaganda.[8] Commercial risks are unavoidable. They can never be eliminated. The role of supervision is to ensure that significant risks are thoroughly and objectively assessed[9] before workers' capital and workers' livelihoods are endangered by reckless, unsupervised, unaccountable decision taking.[10]

To get the debate moving the OECD has to challenge the 'hidden agenda' which still controls the debate on corporate governance.[11] There is an urgent need to look openly and objectively at alternatives to the widely discredited Anglo American model. In doing so it is crucial to ensure that that the interests of workers and all legitimate stakeholders are properly protected. The GLU and its associates need to focus research on how different governance structures rank in terms of protecting corporate wealth. The Anglo American shareholder value model has been extensively researched. In contrast the stakeholder model has not.[12] The research needs to develop appropriate metrics for assessing short and medium term performance in the largest publicly traded corporations, according to governance model in use.

The Anglo American model relies critically on the *Arrow-Debreu* theorem. This demonstrates that *if*[13] the objective of the corporation is to maximise the value of its shareholders, and this is achieved, then it is said to be Pareto optimal. The issue of income distribution is otherwise settled by progressive taxation. This leaves company directors with the untrammelled duty to maximise shareholder value. The pursuit of that objective, it is argued, will in turn promote efficient resource allocation.[14] In contrast corporation law in Rhineland jurisdictions is clear in stating that the objective of the corporation is to promote interests that are wider that simply those of the shareholder[15]. Stakeholder concerns are therefore a central feature of board behaviour and decision taking.

Whilst the stakeholder model this has been discreetly dismissed by as generation of Anglo American corporate financiers and, corporate legal theorists and financial analysts, the tide has eventually turned. We now realise that the Anglo American model of corporate governance fails to meet its single declared objective – maximisation of shareholder value. At the same time it compromises the longer term investment of other stakeholders, most notably working people. Time for the real work to begin to settle the debate once and for all and change corporate governance for the benefit of everyone.

[8] A common argument against duel supervisory boards is that decisions would never get taken and business opportunities would be lost.
[9] There is evidence that bank failures in America and Britain occurred because the advice of risk managers was suppressed.
[10] It is important to remember that all information provided by corporations in Anglo American jurisdictions is *ex post* – after the event.
[11] A reference to the OECD Framework of Corporate Governance and Roundtable discussions.
[12] As quoted in Frank Allen and Douglas Gale: A Comparative Theory of Corporate Governance, Wharton Business School, 2002.
[13] The significance of the **if** is that if the proposition can be effectively contested then the force of much of the argument is lost. The truth of the matter in law is that in Anglo American jurisdictions the fiduciary duty is to the company **NOT** the shareholders which changes radically the justification for its particular portrayal.
[14] A restatement of the now discredited EMH (Efficient Markets Hypothesis).
[15] Specifically research needs to examine the consequences if the objective of the corporation is not, exclusively, to promote shareholder value.[15] In research cited by Allen and Gale *op cit* in excess of 80% of managers surveyed in Germany and France (and Japan) agreed that stakeholder interests are more important than shareholder interests. In contrast more than 80% of British and American managers surveyed saw shareholder interests as being the most important interest.

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