



## Corporate Board Elections and Internal Controls



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### Summing up by Marco Becht, Professor of Finance and Economics, Université Libre de Bruxelles; ECGI Executive Director

We like to close these conferences by doing some summing up, so you don't all go away without having heard some concluding words. Summing up is always a little bit subjective so we'll have two summing ups today so that should then maybe on balance be a bit more objective than if one person does it.

This morning we heard from Thomas Baxter who provided us with a very useful reminder that being in this building is not only very good in terms of the symbolism, this is after all Italian architecture at the heart of the financial district of New York, but that it is also useful in terms of substance because financial regulation is, in fact, a model in many ways or has become a model for corporate governance regulation.

We heard two examples of this. The first was that parts of Sarbanes-Oxley were inspired by financial regulation or the prudential regulation of banks in the United States. In fact, prudential regulation of banks has moved over to the corporate sector. We also heard later on from Chairman McDonough and also from Alex Schaub that financial regulation is also a model for international co-operation in this area. Prudential regulators have a lot more experience in co-operating internationally through the Basel Committee and through other well established fora, especially post-BCCI in regulating banks around the globe. If one regulator has a problem in another country, they help each other and will conduct audits of banks in the home country, being in the country where they actually perform services. With the banking directives and the insurance directives I think we also have a lot of experience on this in the European Union.

Now, let me now turn to some points I took away from the two keynote speakers. The first point I'd like to make is that the ECGI joins the ALI in proposing, if ever asked, that Alex Schaub and Chairman McDonough be awarded the Nobel Peace prize! In fact, we might want to give out the prize ourselves, although that might be bad governance. You can't give prizes to your sponsors. The other thing that struck is what Chairman McDonough stated. He made the following statement, if I noted it correctly. He said, Sarbanes-Oxley is the repudiation of the leadership of the private sector in this area. That's a very strong statement, just to repeat it. He then was quite happy that not only was this happening in the US but also in Europe. He cited Ahold. I'm putting this in his mouth, he's not here anymore, but he was saying that this is also the repudiation of the leadership of the private sector in this area in Europe.

Now, living in Belgium, I'll share with you what some of my Belgian colleagues say - what they tell their children if they really want to frighten them. You have to know that Belgium used to be a Spanish colony at one stage. They say "if you don't behave, we will call the Duke of Alba!". He was the man who had the Spanish Inquisition behind him. So, unfortunately despite the goodwill that we heard both from Alex Schaub and the US regulators, I think in this area we will have underlying tension in this area to continue for the following reason. I think that in Europe, despite Parmalat and the other scandals, we've not yet concluded that the leadership of the private sector has been completely repudiated in this area. In fact, we heard from David Devlin and also from others that there is still a lot of faith in the private sector mending its own way in particular through codes and ,comply or explain, . We heard that in the area of auditing, there is no mandatory regulation in all EU countries. A lot of countries will rely on codes.

Now, even if the European Union decided that it was time to repudiate the leadership of the private sector in this area, the European Union cannot just do this. It is a collective decision-making body of member states and it is unlikely that the 25 will all agree at the same time that it is time to repudiate. The Spanish don't want the Spanish Inquisition and the UK is probably the least likely to agree with this. We heard Turnbull being mentioned. The UK firmly believes that compliance works. Now, this is now. We might have the likes of Robert Maxwell falling off a boat next month, so this might very well change. I can tell you that in Belgium, where I serve on the Corporate Governance Commission which has as one of its purposes to convince policymakers that the private sector can mend its own ways, there was a scandal this year where a controlling shareholder maintained an estate and organised hunting parties at the expense of the public company shareholders. This went down extremely badly with Belgian politicians and we were two inches away from getting Sarbanes-Oxley type regulation in Belgium. So, it is quite possible that individual countries in Europe might move to this but I don't see it happening at the European level immediately. So, this underlying tension I think is going to continue for a while.

The internal control discussion, I found it very fascinating, in particular the idea that now data is coming out on the implementation of this process fascinating. I certainly hope that we will see some research on this in future meetings. I was very interested by the numbers that John Coffee noted and so forth.

I'd also like to draw attention to something that Alexander Schaub stressed a lot in his keynote speech, which is that what Europe is doing now is what the United States did. Light is the best of disinfectants for by now more than 70 years to raise the level of disclosure and you've heard all the directives that are being passed. So, the level of disclosure in Europe is being raised substantially. Now, in this area there will be work to be done to ensure compatibility between these disclosure standards. This was clearly a very important area. There also remains practical work to do. We still don't have a modern version of EDGAR in Europe and all these sort of things but I'm sure this will be sorted out.

I was also struck by the last panel which highlighted one other difference that is there and that will probably continue to cause problems and friction is the different attitudes towards litigation in the US and Europe. We heard this from John Coffee and from the others. I think this is also an underlying fundamental difference that will continue to cause us problems and we should probably discuss this at some stage in the Dialogue.

Turning then to the morning, to the Board elections, I was surprised that as a European observing what's happening in the US that ahead of what the ABA will recommend or whatever, knowledgeable people on this panel said they know, in fact, the plurality voting issue has been resolved and the US is moving to majority voting. That I thought was a major result of this panel. I also thought, looking at this in Europe, we still have in Europe majority voting, proportional voting, plurality voting, co-option. We haven't even started a debate on this. We also have all these complications you heard about, namely co-determination, one share one vote, block holders etc. So, a lot more work in this area clearly needs to be done.

The other theme that came out throughout this panel on Boards was this issue about a collegiate Board versus the political or constituency Board. We heard forceful representations of why the collegiate Board was better and a constituency Board was dysfunctional and could not work because there was confrontation and one could not attract people. Now, let me just add a note to this, a personal note. I was not totally convinced by these arguments. I think that, in fact, the constituency Board is already with us because we've introduced, either through the New York Stock Exchange listing requirements or otherwise, independent directors. In the UK, you have the lead independent director. Now, these people get there through elections but you can only put up certain kinds of people because they have to be independent. So, by definition we already have the constituency Board there.

Finally we heard about family shareholders. I'm sure the Ford family and the Walton family at Wal-Mart maybe want to have a director there to represent the family interests. So, the collegiate Board is fine, but saying that we don't have constituencies is probably not very realistic. Maybe we don't want to have hostile constituencies. What we want is collegiate constituencies.