CORPORATE GOVERNANCE: IMPLICATIONS FROM A CULTURAL PERSPECTIVE

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Abstract

This article aims to research the ample cultural implications behind the expansion and adoption of corporate governance principles and practices and on the cultural differences inherent in the process of translation /localisation of American, English or transnational practices towards continental Europe. More precisely, in the last part of this article, we shall compare the Olivencia rapport from Spain and the Code Corporate Governnace Code of the Bucharest Stock Exchange, with a view to analyzing how elements of national culture influence the transfer of corporate governance principles.

Keywords: corporate governance, cultural differences, Olivencia report, Corporate Governnace Code of the Bucharest Stock Exchange.
JEL classification: G30, G34, G39

1. INTRODUCTION

Corporate governance has become one of the buzz words of recent debates in the broader field of economics. Though the concept is relatively new, with an intellectual history of nearly twenty years only, it gained currency in the context of corporate scandals, transfer of value production from the production activities proper to the risky field of financial speculation, and the ensuing financial crises. If, in the late 1990s, governance was proposed as a new liberal solution to inherent problems of the then developments in capitalism, nowadays, it seems that the solution to cracks in governance systems is more governance.

In the context of the current global economy and increasingly globalizing structures of the social, governance appears as yet another phenomenon that emerged in a particular historical, economical and political context in one part of the world and is now spreading, on globalization's wings, to the entire planet. In geopolitical terms, it emerged in the Anglo-American West and has settled in continental Europe, to colonize the Central and Eastern European countries (the so-called "emerging Europe") and other emerging economies (Brazil, India, Peru, China, Mexico) to expand to the global South [developing countries], with pockets of governance centres and companies that enforce governance practices in Australia and Japan[i].

This article is an investigation into the broader cultural implications behind the expansion and adoption of corporate governance principles and practices, and into the cultural differences in the translation/localization of American, British or transnational practices in continental Europe. More precisely, we shall analyse, in the final part of this article, the Olivencia Report from Spain and the Corporate Governance Code of the Bucharest Stock Exchange from Romania, and assess how elements of the local national culture impact the transfer of corporate governance principles.

2. CONTEXT OF THE EXPANSION OF CORPORATE GOVERNANCE PRINCIPLES

The rise of governance was possible due to the interplay of several political, economic and social-psychological factors. Thus, in political terms first, the phenomenon is part of a broader discursive attempt to combine the neoliberal doctrine with the urge for social responsibility. In the case of corporate governance, this cross-fertilization of ideas constructed "a plausible but intellectually fragile narrative about agency problems and solutions which would align shareholder and management interests" [Erturk, 2004: 677]. This political and discoursive turn occurred after Margaret Thatcher, in Britain, and Ronald Reagan, in the United States, pushed the agenda of the extreme reduction of the presence of the State on the market, of its implication in market mechanisms, of State ownership and State control. The drive for privatization, in England, Reagan's idea that government is part of the problem, not the solution[ii] have paved the way for the doctrine of the "third way," launched in 1997 in Britain and of "compassionate conservatism" in 2000 in the US.

The "third way" doctrine developed by Tony Blair and Anthony Giddens posited the triumph of neoliberalism, the impossibility and futility of resisting globalization and the victorious march of democracy and free-market economics in post-Cold War Europe. It was also built on the presumption that there is a centre-left as a viable political alternative, that is premised on social inclusion and equality of opportunity. A few years later, George W Bush and Marvin Olasky came close to the ideological climate of the "third way" by – unrealistically – envisioning a "'major restructuring of government-societal-religious interactions' which would give churches, mosques and synagogues a much larger role in welfare (Olasky, 2000: 82)" [Erturk, 2004: 682]. This plan, however, was thwarted by first amendment restrictions and the doctrine of separation of church and State.

Olasky's compassionate conservatism and the Blair or Giddens' "third way", share a political rhetoric of openness to change and a preference for indeterminacy in specifying control technologies and in designing their social and political project. It is this indeterminacy, precisely, that created niches and needs for governance mechanisms that would apply to both profit-seeking corporations and public institutions. What is more, the failure of both Blair's promises and of Bush's projects to deliver their highly promoted goals created opportunities for governance mechanisms to be reinforced in companies, universities, hospitals, and volunteer associations.

Economically, the initial promise of corporate governance in the 1990s was backed by the development of the agency theory as a model to explain how modern firms operate on the market and in the broader society. Designed by finance academics to explain firm behavior in the context when owners lack direct control over a company's day to day operations, which are decided upon by the executive manager, agency theory focuses on devising the mechanisms by which corporate managers act in the interests of shareholders. In addition, the theory also gained from reports by well established British businessmen such as Cadbury, Greenbury and Hampel [Erturk, 2004: 684]. These reports refined corporate governance measures, brought into discussion the issue of CEO pay and "fat cat" pay settlements, and set limits on share options in utility companies. The *Combined Code* of good practice for UK corporations turned, in fact, governance into an intelligible phenomenon, whose main tenets are:

- Positive motivation via performance-related management pay;
- Policing of CEO / top management misconduct and increased general oversight of strategy via changes in the composition of the board and proceduralisation[iii].
- Dynamic institutional investors on a proactive capital market who communicate with the management and, if necessary, vote against it [apud Erturk, 2004: 685].

In America, on the other hand, there was already disappointment with governance in the early 2000s, mainly due to the various stages of financialisation. The postmodern corporation no longer add value by creating jobs and actually existing products but by operating on the capital market, undertaking sometimes risky operations, investing the capital of people who have it, so that they could have even more. Thus, through easy gains on the capital market, the gap between the "haves" and the "have-nots" increases, and with it the feeling of injustice and frustration. In the opinion of Erturk *et al.* , this is just natural, and corporate governance is, eventually, a disappointing endeavour "because procedural rules cannot control the self-serving behaviour of social and political elites in the UK and US. If corporate governance was ostensibly about safeguarding shareholder interests, effectively corporate governance sanctioned a huge increase in absolute and relative pay for US and UK top managers who remain the main beneficiaries of governance in a world where the giant corporation has become an important accelerator of inequality" [Erturk, 2004: 677-678].

What was especially regrettable and resented was that the increase in absolute and relative pay for top executives was coupled with dishonest operations, with corruption and bribes, fake reports and paper deals, that could not be backed by companies' actually existing capital. In economics, as well as in politics, in social-psychological terms, these phenomena pointed out to the "corrosion of character[iv]," to use Sennett's term, and the ensuing lack of trust in the economic and political elite, in the new type of economy that emphasizes flexibility, networking, short-term teamwork and corporate re-engineering.

3. EXPORTING CORPORATE GOVERNANCE: CHALLENGES AND THE RELEVANCE OF CULTURE

The Cadbury report from 1992 launched the term "better governance," which was quickly integrated into a powerful promise. By the late 1990s, reports from the World Bank and the International Monetary Fund preached that the entire planet would fare better if other states/corporations/institutions adopted the techniques of Anglo American corporate governance. Though much praised, in theory and politics, these systems were soon to prove their failure to prevent or detect dishonest, disloyal and irresponsible behaviour in companies like Enron or World Com in the United States, while in 2003 the British media voiced its outrage over high executive pay packages or over 'rewards for failure'. For most scholars, the solution to problems of governance systems is more governance, as if to paraphrase

John Dewey's famous saying that the solutions to problems of democracy is more democracy.

The remainder of this article is in investigation into the cultural assumptions implicit in the corporate governance philosophy and into the challenges that local cultures pose to the translation/localization of corporate governance structures and practices. The starting point of our analysis is the OECD *Principles of Corporate Governance,* endorsed by the member countries in 1999 and henceforth, "an international benchmark for policy makers, investors, corporations and other stakeholders worldwide" [2004: 3]. The revised version, based on the analysis of challenges posed by the adoption of these principles and both member and non member countries, was subsequently accompanied by a *Methodology for Assessing the Implementation of the OECD Principles of Corporate Governance* [2007]. We shall analyse how these principles were recontextualized in Spain and Romania, by focusing on two documents: the *Report by the Special Commission to Foster Transparency and Security in the Markets and in Listed Companies*, also known as the Olivencia report, from 2003 and the *Corporate Governance Code of the Bucharest Stock Exchange*, from 2008.

3.1. DIMENSIONS FOR THE ANALYSIS OF CULTURE IN A BUSINESS CONTEXT

In a classical definition, culture is the "software of the mind[v]" – the underlying patterns of thought and feeing that are mutually shared among members of the same culture and that influence the way in which they act in the world, the decisions that they make and the priorities that they have. In his work with IBM employees, Hofstede identified four dimensions along which cultures differ, to which he added a fifth one, later. These dimensions are:

1. power distance: cultures are classified as having a low power distance index or a high power distance index depending on how flat or high their hierarchies are. The American, Canadian and Scandinavian cultures are at the low end of the continuum, while Arabian, Latin American, Russian, Indian and Chinese cultures are at the high end of the continuum.
2. individualism: national cultures are classified as being individualistic or collectivist depending on whether they value and cherish the individual or the group. Individualist cultures, such as those of Northern America and Western Europe, put a premium on personal achievement at the expense of group goals, and encourage fierce competition. Collectivist cultures, such as those of China, Korea, and Japan, cherish family as a cultural value and work-group goals.
3. masculinity: cultures are classified as masculine or feminine depending on the predominant gender roles and correlated values that can be seen in society. Thus, in a masculine culture, there is a strong spirit of competition, personal achievement, interest in the accumulation of wealth; feminine cultures, on the other hand, appreciate modesty and care, have a nurturing attitude towards people and emphasise harmony rather than competition.
4. Uncertainty avoidance: this index reflects a culture's tolerance for ambiguity and the unknown. High uncertainty avoidance cultures minimize the discomfort of the unpredictable by designing strict laws and rules, creating codes of conduct and concluding exhaustive contracts; low uncertainty avoidance cultures have a certain tolerance for the unknown, and are more tolerant of opinions and practices that differ from theirs.

5. long term orientation versus short term orientation refers to how far away in the future one sets his or her goals, and to how long one can postpone the gratification of achieving one's goals[vi]

Apart from Hofstede, another theoretician of culture whose work has been influential in the cultural analysis of businesses is Edward T. Hall's *The Silent Language* [1959] where he introduced two fundamental distinctions: one, between monochronic and polychronic cultures [i.e. cultures in which people engage in one activity at a time and cultures in which people engage in several activities in parallel], and the other one, between low context and high context cultures. In the case of the former, the amount of information that is mutually shared is large. In the case of the latter, it is low, and what is not shared needs to be spelled out.

3.2. CORPORATE GOVERNANCE CODES AS CULTURAL DOCUMENTS

We suggest that corporate governance codes can be interpreted as cultural artifacts along the cultural dimensions mentioned above, and that when one transnationally-developed code such as the *OECD Principles of Corporate Governance* is to be enforced in a particular national context, the local culture is likely to pose challenges to the process.

A close reading of the *OECD Principles of Corporate Governance* reveals the following cultural features:

- the *Principles* attempt to reduce the power distance between agents [executive management] and the owners [shareholders] by creating the mechanism through which the former's authority based on expert knowledge is reduced;
- against the pursuit of individual gains, it creates a system whereby executives are bound to work for the benefit of the collective of owners, as well as of other stakeholders in the firm. This, the ethos of corporate governance is collectivistic rather than individualistic;
- they emphasise the feminine values of care and protection, to counter the masculine spirit of competition and pursuit of personal gains. Chapter II *The Rights of Shareholders and Key Ownership Functions,* specifies that "the corporate governance framework should protect and facilitate the exercise of shareholders' rights," and chapter III emphasizes the need to ensure "the equitable treatment of all shareholders, including minority and foreign shareholders", as well as the effective means of redress, should they have been victims of abuse.
- In terms of uncertainty avoidance, though the *Principles...* stipulate specific cases that have to be considered [shareholder rights and equitable treatment, role of stakeholders, disclosure and transparency, responsibilities of the Board], the language used is rather vague and it leaves room for interpretations. We argue that uncertainty avoidance is at an average level.
- The principles have a long-term orientation, that is polychromic in the simultaneous urge to consider both shareholders and stakeholders.
- The indeterminacy of terms makes us consider it a low context document.

When we analyse instances of corporate governance codes at national level, their features as cultural documents vary depending on the particular context in which they were proposed for implementation. Thus, the so called Olivencia report, the first attempt in Spain to establish a Code for Good Corporate Governance, in 1998, followed by *Report by the Special Commission to Foster Transparency and Security in the Markets and in Listed*

Companies in 2003 and the Principles of Good Corporate Governance: Code of Good Practice for Boards and Directors, published by Instituto de Consejeros Administradores in 2004 and 2005, are more exhaustive and specific. The first document, created on the basis of thorough analysis of American and British corporate governance practices, spelled out what was shared knowledge in the American low context.

In a very thorough investigation of the Olivencia report, Sison specifies that the document, initiated by the public sector, could be carried out only with governmental support. It was designed at a time of increased privatization and under the both internal and European pressure for reforms, and it was meant to function as a useful instrument for companies undergoing privatization. It is manager-friendly, and puts a premium on shareholders' interests rather than on stakeholders, in comparison with other American, British and French codes that the author analyzed, and that made more room for stakeholder interests. The difference in this approach translates as follows: "whereas the stockholder mentality emphasizes return on equity, productivity, innovative technology and competition, the stakeholder mindset underscores wages, job security, environmental safety and social cooperation" [Sison, 2000: 184]. Other sites of difference between Spanish corporations and their American and British counterparts refer to the stock options that are available to executives: in the US, the percentage of shares an executive can receive is high, whereas in Spain it is very low. Also, whereas American companies make an average of 10 % of their stocks available to their employees, in Spain, at the time when the code was created, offering shares to employees was the exception and not the rule. In addition, in terms of board structure, the specific feature of Spanish boards is their youth and relatively high ethnic homogeneity, with a very low percentage of foreigners acting on them.

Sison takes issue with the major values that are enforced by the Code for Good Corporate Governance in that their vagueness and decontextualisation can be problematic. The three values that he analyses are loyalty, due diligence and transparency. First, loyalty is bound to create problems because the term/concept does not exist in the abstract. One is loyal **to** someone else, or to one's self, depending on the values inherent in his or her culture. As Sison points out, family ties are extremely important in Spain, therefore one is naturally inclined to place his or her allegiance to one's family rather than to one's company [Sison. 2000: 188].

Second, "due diligence" is seen in a double interpretation. In a positive meaning, it refers to good faith, prudence and professionalism; in a negative meaning, it refers to the fact that boards "are not a social club" [Sison. 2000: 189] made up of straw-men who are there only for the sake of complying with the legal requirements that insist on the existence of boards, and who approve everything that management decides, or that the major owners, i.e. the founding family, wishes to achieve. Yet, in practice, the major decision power remains with the founding family. In addition to this, Sison draws the attention to the cross-dictatorship prevalent among major Spanish financial industrial groups [Sison. 2000: 189].

Third, transparency refers to the type of standard information that is made available to all stakeholders and shareholders, and to the amount of it. Knowledge and information are sources of control, as well as profit opportunities. Spanish companies, at least at the time when the Code was designed, were extremely secretive and this cultural feature posed challenges to the culture of transparency and average uncertainty avoidance promoted by the ideology behind corporate governance principles.

If we analyse the Corporate Governance Code of the Bucharest Stock Exchange, we can notice that it aims to incorporate the OECD principles and make them explicit for Romanian companies. It emphasizes clarity and transparency in corporate communications with the shareholders and the stakeholders, the fair treatment of shareholders, their right to express their opinion, be informed via a special section on the company's website and participate in decision-making. The Romanian Corporate Governance Code aims to create a culture of accountability, transparency, participation and sustainable development, in a long-term cultural orientation. It is careful to establish the right distribution of executive and non-executive board members, lest a fraction would gain control and more decision-making power. It also puts a premium on corporate social responsibility, on fair board nomination, self-evaluation and "appropriate" remuneration.

The Code, vague as it may be at points, sounds extremely well. Unfortunately, it is, for the moment, a discoursive exercise, since only one Romanian company has managed to adopt it. This failure of implementation comes, we believe, from both economical, historical and cultural specificities. In the recent Romanian history, under communism and in the post-communist age, transparency has never been a cherished value. The control-based communist system indirectly encouraged people to hide from authorities and keep information private; enterprises were reporting cooked production figures, just like, in the post-communist age, a lot of economic activity developed underground, on the grey market. Another point that needs to be highlighted is that the Code also emphasizes punctuality of reporting, preciseness, and an ethos of accountability that is not familiar to the local national and business culture.

4. CONCLUSIONS

Enhanced governance mechanisms and the expansion of governance principles are preached nowadays as solutions to the financial and economic crisis, and as preventive measures lest such a crisis should occur again. Briefly stated, governance mechanisms are meant to ensure that managers act in the shareholders' interest and they receive appropriate performance-related pay. The spread of governance structures and of the philosophy behind them goes hand in hand with globalization and with the transfer of American and British practices towards the rest of the world. This process of transfer and trans-lation of corporate governance principles is neither smooth, nor standardized. In this paper we have argued that the localization of governance principles, as well as the enforcement of governance principles once they have been spelled out, are influenced by the dominant values of the local culture and by local *habitus*. Thus, as we have seen in the case of Spain, the premium put on family values can be an obstacle to the principle of shareholder and stakeholder loyalty; or, as we have seen in the case of Romania, transparency is hard to be enforced since it has not been part of the recent ethos of neither the nation nor businesses. Yet, unlike Erturk e*t al*., we do not believe that corporate governance must disappoint. We think that, in time, corporate governance mechanisms and structures can be internalized if people learn and experience their benefits, if they themselves perceive the need for renewal and reform of character.

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[1] UTS (University of Technology Sydney) Centre for Corporate Governance, for instance, is a leading research institute dedicated to the study of corporate governance structures and processes from an interdisciplinary perspective. Japanese universities have graduate programmes and courses in governance, developed nationally or in partnership with American universities.

[2]This idea ("In the present crisis, government is not the solution to our problem") was mentioned in his inaugural speech in January 1981, available at http://www.bartleby.com/124/pres61.html)

[3]In the UK, Cadbury initiated the separation of chairman and CEO positions and emphasized the role of independent non-executive directors. Proceduralisation was represented via remuneration and audit committees that , according to Hampel, should consist exclusively of non-executives.

[4]*The Corrosion of Character: The Personal Consequences of Work in the New Capitalism*, published in 1998, is a classic work that analyses changes in the social psychology of workers in the so-called New Capitalism/Neoliberalism of the 1990's.

[5]The term was coined by Hofstede in his *Cultures and Organizations: Software of the Mind*.

[6]For more detailed information on Hofstede's cultural dimensions and national indexes, see http://www.geert-hofstede.com/geert_hofstede_resources.shtml