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## The Transformation of Corporate Governance Regulation in Europe - Towards a Marketisation of Corporate Control?

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## **Abstract**

The transformation of corporate governance has only recently come into the focus of the academic debate on the transformation of the varieties of capitalism in the European arena. While most studies still are either focused on a comparative analysis of the transformation of national systems of corporate governance or rather technical aspects of the changing configurations and mechanisms of corporate governance, analyses of the ongoing transformative political processes on the European level are still scarce.

This research project is aimed at shedding some light on the often neglected essentially political dimension of the transformation of corporate governance regulation in the European Union. While to a certain extent drawing on the Varieties of Capitalism approach, the focus of this research is none the less not merely comparative. Rather, this research seeks to map out and explain the transformative processes of corporate governance regulation - in particular with regard to the market for corporate control as an important element of corporate governance - within the context of the European integration project. It does so by drawing on an analysis of these transformations which moves beyond state-centred and rational-choice accounts by paying attention to transnational actors as well as the structural factors that influence them and are in turn shaped by them. The struggle over the European Takeover Directive will serve as an empirical focal point to analyse the role of the EU in creating a European market for corporate control.

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## 1 Introduction

Corporate Governance, which has become a buzzword both in the public and academic debate, is of fundamental significance for the socio-economic configuration of capitalist modes of production. Corporate governance regulation by now is an issue of heated debate in any industrialized country, and the reverberations of these transformations can easily be traced back to everyday life. Yet with all the buzzing going on, it seems that the political nature and underpinnings of any corporate governance system have become obscured, if they have ever been observed at all.

Within the European Union, we are witnessing a transformation of corporate governance regulation which is apparent not only on the various national levels, but also on the European level per se. The political processes that bring about these transformations, however, have hardly been accounted for – only recently have scholars begun to pay attention to them (Bieling and Steinhilber 2002; Cioffi 2002; Gourevitch 2003; Roe 2003). Yet whereas the majority of political science studies is so far still focused on the transformation of national systems of corporate governance (see f.ex. Frentrop 2002; Höpner 2003b), most legal and business studies scholars take a rather normative stance on corporate governance by analysing the transformation of corporate governance on the grounds of finding the ‘best practice’ - which for most of them, incidentally, tends to be of the market-based Anglo-Saxon sort. (Bergloef and Burkart 2003; Cuervo 2002; Hansmann and Kraakman 2001).

A common objective of many scholars seems to be to participate in the pick’n mix of the convergence debate, which appears to constitute the ultimate purpose of many studies of the transformation of corporate governance regulation. Whether there is indeed convergence on a specific corporate governance regime or whether the varieties will, at least to a certain degree, persist is, of course, of immediate importance for the development of capitalism in Europe and elsewhere. Yet it has hardly been investigated *why* these processes take place. Instead of resorting to simplistic causal models on the grounds of ‘globalisation’ and competitive pressures (or, for that matter, path dependent outcomes), the political processes behind these transformations have to be the focus of an analysis.

Within the framework of ARCCGOR, this research project aims at contributing to the academic debate by not buying into the somewhat outcome-oriented focus of already existing studies of the transformation of corporate governance in Europe (Cernat 2004; Lannoo 1999; Reberieux 2002). Rather, the underlying research question will be based on the one posed by Nölke, Overbeek and van Apeldoorn (Nölke et al. 2003) in their initial outline for the ARCCGOR programme - *What explains the transformation of corporate governance regulation at different levels, and through varying modes, of governance?*

In the following, then, I will map out the structure and the research objectives of my project. A brief overview on the various strands of literature on corporate governance in general and the market for corporate control in particular provides the basis for a discussion of the ‘state of the art’ and the identification of important gaps and neglected issues in the existing literature.

In turn, the scope (and limits) of my research project will be outlined, in particular with regard to my main empirical focal point, the Takeover Directive. To locate my project in the academic debate and to point out its potential contribution to the study of corporate governance regulation in the European Union, a first sketch of my theoretical framework with a clarification of some key concepts this research is drawing on will conclude this research outline.

## **2 Corporate governance and the market for corporate control revisited**

*There is no longer any serious competitor to the view that corporate law should principally strive to increase shareholder value (Hansmann and Kraakman 2001: 439)*

Many scholars, in particular in legal and economic fields, still take corporate governance to be a mere mechanism to overcome arising agency costs due to the separation of corporate ownership and control (Berle and Means 1991 [1932]) – in short, ‘how investors get the managers to give them back their money’ (Shleifer and Vishny 1996: 4). The firm or company, in this perspective, is nothing else than a ‘nexus of treaties’ (Jensen and Meckling 1976: 8), an act of rational actors to guarantee an efficient (re)allocation of wealth by overcoming transaction costs (Coase 1937: 389). The company’s main purpose, thus, is to maximise the cash flow to the shareholders (the bearers of residual rights) – giving rise to the concept of shareholder value (Rappaport 1998). Any management focus on other stakeholders such as, for instance, employees poses a potential threat to this cash flow and has hence to be avoided.

Few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible (Friedman 1962: 133).

The market for corporate control (Manne 1965) features prominently in this perception of corporate governance as control mechanism to mitigate agency problems - it constitutes the primary external control mechanism to ensure the protection of shareholder interests. Based on the premise that there is a high positive correlation between managerial efficiency and the share price of a company (Manne 1965: 113), the market for corporate control not only serves as disciplining mechanism for managers, but also gives shareholders an increased ‘exit’ option, i.e. to sell their shares. (see Hirschman 1970) A functioning market for corporate control thus aligns managerial strategies with shareholder interests (‘maximizing shareholder value’) rather than taking any other socio-economic interests into account. The evaluation of company performance takes place on the grounds of market-based criteria - in the case of a takeover, ‘shareholders are not asked to evaluate complex alternative business plans for the company. Rather, they need only assess who is offering a higher value for their shares’ (Pound 1993: 1018). Both technical defences against takeovers, such as attempts to make the target company’s stock less attractive to the bidder (‘poison pills’) or the selling of valuable assets (‘scorched earth’),<sup>1</sup> and structural obstacles impeding the functioning of the market are thus perceived as

detrimental to shareholder interests.

This distinction between structural vs. technical barriers to takeovers is important for the discussion of takeover regulation. As Gilson points out,

structural barriers simply reflect the effect of existing conditions in the economic environment, albeit facilitated and reinforced by conditions in the corporate governance and political environments. They include such circumstances as the concentration of ownerships and small groups, the influence of large banks and the reliance on debt as opposed to equity financing (Gilson 1992: 181).

These structural barriers thus pertain to the different socio-economic configurations constituting the various corporate governance systems and varieties of capitalism in general. The market for corporate control, however, is far from being a universal feature of corporate governance systems. Whereas corporate takeovers have been and still are common in the US (see f.ex. Blair 1993 on the 'Deal Decade' in the US in the 1980s), the absence of a market for corporate control has been a distinct characteristic of various 'continental' corporate governance systems (de Jong 1997; Streeck 2001).

### **3 Approaches to corporate governance**

#### **3.1 Legal perspectives**

The differences between corporate governance systems, of which the market for corporate control constitutes a significant element, have increasingly been subject to academic debate between various fields. There is a prominent strand of (predominantly American) legal and economic scholars arguing for the convergence of corporate governance systems on the above shareholder-value model (see Gordon and Roe 2004) – Hansmann and Kraakman (2001) have even pronounced the 'end of history of corporate law,' claiming that the pressure of increasingly globalised markets, the rise of institutional investors and the sheer superiority and efficiency of the shareholder value model will inevitably lead to a global convergence on the prevailing model, with any divergent models of economic organisation and corporate governance bowing out to ruthless competition.

Comparative corporate governance has become a popular subject for both social sciences and legal studies (O'Sullivan 2003), yet there is still an underlying normative bias assuming that corporate governance will necessarily converge on the most efficient system (see for instance Shleifer and Vishny 1996). As Branson puts it, 'they construct competing models based upon a limited sample of on the one hand the United States and , on the other hand, the UK, Germany and France. They then declare the United States the winner of the competition' (Branson 2001: 335).

Although there have been attempts at more complex explanations for the diversity of corporate governance systems, ultimately these fail to account for the underlying political dimension of corporate governance. La Porta et al, for instance, having conducted extensive research on

the structures of corporate ownership in various advanced industrial countries worldwide (La Porta et al 1999), introduce the structure of company law as a variable influencing corporate governance regimes. They conclude that strong investor protection by law (as provided for by common law countries like the USA or the UK) facilitates efficient corporate governance (La Porta et al 2000). They do not, however, acknowledge the political processes and institutional configurations underlying the emergence and persistence of a particular company law regime – thus, changes and transformation of corporate governance systems are still explained by exogenously induced changes in (corporate) law (in terms of ‘globalisation pressures’).

The notion of ‘the political determinants of corporate governance’ has been introduced by Mark Roe (Roe 2003). He argues that political forces bring about specific corporate governance systems by being the primary determinants of the degree of shareholder diffusion and the relations between managers, shareholders and other stakeholders (Roe 2000; Roe 2003). This is a crucial insight, and Roe’s path-breaking work in this direction constitutes an important improvement on the ‘legal’ account of differences in corporate governance systems (cf Gourevitch 2003). Yet while Roe takes the degree of ‘social democracy’ as one of the main factors influencing corporate governance systems through generating low shareholder diffusion and weak shareholder rights (cf La Porta et al. 2000; Roe 2003: 37), he bases his account on a very narrow political interest coalition between managers and employees against shareholders. He argues that ‘social democracies wedge open the gap between shareholders and managers in public firms, by raising agency costs and reducing the efficacy of techniques that would control them’ (Gordon and Roe 2004: 290). This static perception of fixed interests in corporate governance systems is, however, ultimately insufficient for explaining the transformation of corporate governance since it simply doesn’t account for the political interests and changing power relations between these different actors and the changing outcomes of these processes. To identify the various actors involved in processes of corporate governance and to not only distinguish their particular agenda, but also the underlying forces shaping them serves to (re)politicise corporate governance. This is based on a perception that, rather than being a mere control mechanism for shareholders or managers, corporate governance is an area of very concrete political contestation.

### **3.2 Of varieties and other capitalisms**

Roe’s perception of the ‘political determinants’ in continental Europe in terms of ‘social democracy’ as institutional arrangement impeding the resolution of ‘the core problems of the public firm [i.e. agency problems, LH]’ (Gordon and Roe 2004: 252) correlates to a certain extent with another approach focusing on the significance of institutional arrangements, namely the burgeoning literature on the varieties of capitalism (VoC).

Within this by now extensive literature, corporate governance constitutes an essential element of the institutional configuration of capitalist economic organisation (Hall and Soskice 2001: 23-24). The debate around the different varieties of capitalism was triggered off by

Michel Albert's popular account of the struggle of 'capitalism against capitalism,'<sup>2</sup> in which he identified the fundamental differences of varieties of capitalism and argued that the 'Rhenish' model of capitalism, which was predominant in continental Europe, would eventually be superseded by the 'Anglo-Saxon' model (Albert 1991). The VoC has since become an important branch of the social sciences, and although it is far from being a coherent and unified approach, there are important overlaps and similarities in the various contributions to it. (see f.ex. Amable 2000; Aoki 2001; Berger and Dore 1996; Crouch and Streeck 1997; Hay 2000; Kitschelt et al. 1999; Whitley 1999) In marked contrast to much of the economic and legal literature mentioned above, the VoC is not based on any normative assumptions of the superiority of any model, thus discarding with the view that (institutional) convergence can lead to some sort of 'best practice' model of capitalism. Rather, on the basis of ideal-types of capitalism it is pointing towards the inherent institutional features of the various models. For this purpose, the notion of 'institutional complementarities' is of utmost significance (Hall and Soskice 2001: 17). As Crouch and Streeck contend, 'the failure to recognize the role of institutions may lead, and indeed is currently leading, to the false conclusion that markets alone can sustain economic dynamism' (Crouch and Streeck 1997: 7).

By setting corporate governance within the context of a broader institutional configuration, the VoC allows for a more systematic analysis of the significance of corporate governance for socio-economic organisation. From this perspective, the absence of a market for corporate control, for instance, constitutes a comparative advantage with regard to the development of a highly qualified labour (Streeck 2001). The attention the VoC is paying to the different institutional arrangements necessarily leads to its overarching research focus on the diversity and the differences between national forms of capitalism. With regard to the question of the political dimension of corporate governance, however, this comparative focus entails the problem that, in Susan Strange's words, 'they don't see the wood for the trees, [and] overlook the common problems while concentrating on the individual differences' (Strange 1997). Drawing on historical institutionalist and comparative politics approaches, the VoC also very much remains ontologically tied to the nation-state.

Many of the most important institutional structures, notably systems of labour market regulation, of education and training, and of corporate governance depend on the presence of regulatory regimes that are the preserve of the nation-state (Hall and Soskice 2001: 4).

This, in turn, also prompts a predominant focus on state actors' interests when discussing the transformation of the regulative environment of corporate governance. (Hall and Soskice 2001: 57). This, it could be argued, leads to a strong intergovernmentalist bias when identifying the actors involved in the politics of corporate governance regulation – the VoC cannot account for supra- or transnational actors. In concert with the rather US-centred focus of the other approaches mentioned above, this means that there is a clear gap in the literature with regard to the international and transnational aspects of the transformation of corporate governance.

Pertaining to the question of changes in corporate governance regulation, the concept of path-dependence is of great significance to account for the persistence of institutional configurations such as corporate governance regimes (Bebchuk and Roe 1999; Greener 2004; Pierson 2000). As Bebchuk and Roe contend, 'the corporate structures with which a country began will influence those that it will have down the road' (Bebchuk and Roe 1999: 129) This relates to the historical institutionalist account of the VoC, which asserts that national models of corporate governance react differently to exogenous pressures. To explain these different outcomes, the VoC draws to a large degree on path dependency to reveal the historically specific cultural, economic and social configuration of any variety of capitalism (cf Hall and Soskice 2001). The considerable diversity with regard to corporate governance practices, in this view, is thus mainly based on the path-dependent nature of these regimes. The insight that the institutional history of corporate governance is of vital significance for its development is, as such, very important - not only that 'institutions matter' (North 1991) but also that timing and 'history matters.' 'Locked into' their specific institutional configurations, corporate governance regimes are thus, from a path-dependency view, likely to persist even under increased pressure from external forces. Yet ultimately, path dependency can not account for transformations such as those within the area of European corporate governance regulation. As Federowicz and Aguilera point out, in 'post facto explanations everything might be interpreted as path-dependent, but it offers little insight into the mechanisms of institutional change (Aguilera and Federowicz 2003: 5). Whereas path dependency can offer an explanation for institutional inertia within a given context of a national institutional constellation, it does not have an answer to transnational political processes such as supranational EU regulation. Also, the perception of path dependency as mechanically pressing institutional development on a certain trajectory does not leave enough room for the contingent and conscious agency of actors, both from within the institutional context and from outside. Peter Gourevitch argues that 'there is nothing inevitable about a country's path, nor is it locked in forever. Its trajectory is sustained by interests, ideology and institutions - each of which can change' (Gourevitch 2003: 1866).

With respect to the literature on the transformation of corporate governance on the European level, there has been a welcome increase of scholars taking on this issue from various perspectives. (Bieling and Steinhilber 2002; Cernat 2004; Cioffi 2002; Dewing and Russell 2004; Höpner 2003a; Lannoo 1999; Lannoo and Khachaturyan 2003; Reberieux 2002; Rhodes and Apeldoorn 1998; Streeck 2001; van Apeldoorn 2001) The ongoing changes and rapid developments of corporate governance regulation in the European Union are under increasing attention from scholars from both political science as well as legal/economic fields - given the significance of corporate governance, this development is quite likely to continue. To this date, however, there is no coherent systemic account of why the regulation of corporate governance in the EU is developing the way we can observe (neither, for that matter, is there agreement in what we actually observe with regard to corporate governance in the EU) Globalisation pressures still lead the way as explanation for the transformation of corporate governance

regulation, albeit with very different outcomes (Lannoo 1999; compare f.ex. Streeck 2001).

The qualitatively changed *content* and the underlying political reasons for the qualitatively changed *form* of regulation are systematically neglected (but see Bieling and Steinhilber 2002). Rather than a descriptive account of which processes are taking place at different levels, what is needed is an approach to identify on the one hand the transnational character of these processes, which cut through the various layers of governance and ‘take place in *several national contexts simultaneously*’ (van Apeldoorn 2004: 145, emphasis in original), as well as to *explain* their form and content with regard to the underlying political project.

There is, then, an apparent need for a study of the transformation of European Governance which takes into account not only the political dimension of corporate governance regulation, but also the evidence of transnational forces that sustain corporate governance transformation, such as for instance transnationally mobile institutional investors or ‘private’ expert groups involved in agenda setting.

#### **4 Corporate governance in the European Union - developments and research scope**

In the last couple of years, there has been an increasing number of indications that a market for corporate control is emerging in Europe (Höpner and Jackson 2001; Lannoo 1999; Lannoo and Khachaturyan 2003). The volume of unsolicited takeover bids in the EU has been increasing steadily, and the number now actually surpasses the number of takeovers in the US (Wells and Saigol 2004). The Financial Services and Action Plan (FSAP) (European Commission 1999) outlines a broad restructuring of European financial markets to advance the further integration of the single market. The Takeover Directive has to be seen as an integral element of this framework, as the Commission points out in the FSAP.

The proposal for take-over bids (13<sup>th</sup> Company Law) Directive will facilitate the restructuring of the financial industry – a process which has been gathering pace- and mark an important milestone in the emergence of an open market in EU corporate ownership (European Commission 1999).

The deepening of European capital and financial markets is an essential prerequisite for the emergence of a market for corporate control. While the market for corporate control constitutes a distinct market from the markets for goods, land, labour and capital (Windolf 1994), it is none the less dependent on a functioning capital market since corporate control is inextricably linked to vote-carrying securities traded on capital markets. It is crucial with regard to this project, thus, that research on the emergence for a market of corporate control in the EU can not simply focus on the Takeover Directive alone, but also has to be concerned with the integration of capital markets which are necessary to bring it about. With regard to the theoretical framework of this research, I will argue below that this facilitates setting the Takeover Directive and the push for a market for corporate control into the broader picture of a political framework for the integration of financial markets in the EU (cf Bieling and Steinhilber 2002).

At the same time, however, European company law is still predominantly determined at the national level, and various institutional arrangements render takeovers less likely (and less desirable) in some member states, while corporate control in other member states is far more marketised (Heine and Kerber 2002). This gives rise to regulatory tensions which constitute an inherent element of the political struggles over corporate governance regulation in the EU.

In the following, I want to give a brief overview of the developments around the Takeover Directive, which then serves as an illustration of the research scope and some of the issues and tensions that form the empirical part of this project.

The EU Commission has been pushing hard for its Takeover Directive, which, after many years of struggle and a crushing defeat in the European Parliament in 2001, finally came into force in May 2004, albeit in a diluted compromise form. Whereas the directive started off in the 1980s with the objective to harmonize takeover regulation (see the explanatory memorandum of the 2002 proposal, European Commission 2002), in the course of the negotiations with the European Parliament (EP) and the Council it gradually shifted away from ‘one size fits all’ harmonization towards more market-driven and self-regulated mechanisms. Rather than introducing strong regulation to bring about harmonization, the Commission thus took a more pro-competitive and proactively market-opening stance (what Fritz Scharpf would call ‘negative integration’ (Scharpf 1999: 45). In its 2001 proposal for the directive, the Commission had introduced the ‘board neutrality rule’, which required the target company’s board to get the shareholders’ permission for enacting any measure which could result in a frustration of the bid. The rejection of this proposal in the EP in July 2004 was, among other reasons, based on the perception that with the diverse models of company law in the EU, the board neutrality rule would disadvantage member states where structural barriers against takeovers were not in force.<sup>3</sup> This lack of a ‘level playing field’, i.e. equal opportunities for takeover bids and shareholder decision-making, was perceived to be the biggest obstacle to European takeover legislation. The Commission, however, did not discard its plans for the takeover directive and commissioned a High Level Group of Company Experts (HLG) to tackle the problem of the level playing field. The HLG presented its report on takeover bids in January 2002 (High Level Group of Company Experts 2002), in which they devised the ‘breakthrough rule’ as a solution to the problem of the lack of a level playing field. This breakthrough rule would quite literally enable a bidder to ‘break through’ structural pre-bid barriers like multiple voting rights and voting restrictions once a certain threshold of control over the target company has been reached. This would result in a playing field which would, at least temporarily in case of a bid, provide bidders for a company under this regulation with a barrier-free target company. At the same time, the shareholders of the company, under the board neutrality rule, would ultimately decide on whether to accept the bid. Taken together, this would result in a level playing field with ultimate shareholder decision-making, as envisaged by the Commission. Yet, since the Commission expected considerable opposition from member states where structural barriers constituted an integral part of company law, it only drafted a ‘mini breakthrough rule’ in its 2002

proposal for the takeover directive (Dauner-Lieb and Lamandini 2002; European Commission 2002). This, however, led to heated debates and negotiations in the Council and the EP over the issue of the level playing field again. In the end, a compromise drafted by the Council was supplemented in the directive, which renders the board neutrality rule and the full break-through rule optional under the authority of the member states. This compromise directive was thus accepted by the EP in December 2003 and has come in force in May 2004 - much to the disappointment of the Commissioner for the Internal Market, Frits Bolkestein, one of the most outspoken advocates of European takeover regulation. After the directive was accepted, he was adamant in his criticism:

I am not going to pretend that I am pleased with this agreement. Nor am I going to be hypocritical by pretending that the version of the Directive agreed today represents a step forward for EU competitiveness or for the integration of EU capital markets (Bolkestein 2003).

The directive will have to be implemented into national law by the Member States by may 2006 – until then, it remains to be seen to which extent the optional arrangements will be enacted. Also, the directive will be subject to revision in 2011.

## **6 Research interests and questions**

Drawing on the above descriptive delineation of the scope of this research project, I now want to introduce some of the relevant and highly interesting issues which, from a political economy perspective, pertain to corporate governance regulation in the EU in general, and takeover regulation in particular. Subsequently, I will submit the general research questions underlying this project, as well as some of the limits of this project. In turn, a first sketch of my theoretical framework will outline how I intend to go about interpreting and analysing these research problems as well as operationalising my research questions.

While many studies of the transformation of European corporate governance are rather outcome-focused, this project departs from the position that, rather than merely analysing the *results* of changes in regulation, the research focus of this project will be on *how and why* these transformations take place. This can only come about by, to a certain extent, historicising the events and changes in corporate governance regulation. The ‘endless saga’ (Skog 2002) of the Takeover Directive, for instance, can not be understood outside the very specific context of the integration of the European Single Market. Also, it is crucial to contextualise it within the broader setting of the development of company law in Europe. The shift from the Commission’s initial position to a more market-driven approach, the repeated contestation of the Directive in the EP and the Council and the eventual coming into force of the Directive pose complex questions about the *cui bono* of takeover regulation. One of the main issues is in whose interest this specific form of takeover regulation would be, and which actors in turn advocate these interests. In this regard, the role of the Commission in pushing the directive based on the thrust of a larger project of European (market) integration will form an integral part of the research

focus.

It is also crucial to analyse in how far the form and the content of the Directive and other transformations are *interrelated*. With regard to changes in the content of regulation, the shift towards pro-competition and increasingly process-oriented provisions instead of harmonizing and institutionalizing measures has to be accounted for. With regard to the form, the use of consultancy terms such as benchmarking of corporate governance codes to arrive at a 'best practice' fosters this change of corporate governance regulation by furthering the tendency towards self-regulation which is an inherent feature of market-oriented corporate governance. Also, the changing modus for regulative processes, as with for instance the Lamfalussy Process or the increased use of expert groups to advance certain positions (e.g. the High Level Group of Company High Level Group of Company Experts 2002) will be part of the research focus. With regard to the latter, it is essential to analyse in how far these 'neutral' experts actually influence and set the agenda for political processes and decisions on corporate governance regulation.

Although, as mentioned above, the overarching focus of this project is on why transformations in corporate governance regulation take place, it will nonetheless be essential to first identify the changes and evaluate in how far they entail a significant shift from the hitherto diverse European landscape of takeover regulation, company law and varieties of capitalism in general to a different form – whether this will turn out to be a process of convergence, persistence or hybrid formation remains to be seen.

Drawing on these concerns, the *central research questions* for this project are outlined below.

- *What changes in the regulation of corporate governance can we observe in the European arena, in particular with regard to the emergence of a market for corporate control?*
- *How and through which modes of regulation do these changes take place? Do they imply a shift from public to private actors, for instance the High Level Group of Company experts?*
- *What accounts for the transformation of corporate governance regulation in both form/modus and content? In particular, what is the role of the EU in creating a market for corporate control in Europe?*

The Takeover Directive, as one of the prime efforts of the Commission to advance a European market for corporate control, is a particularly apposite and interesting focal point for the study of the transformation of corporate governance in the EU. At the same time, however, the limits of this research project have to delineated, also with regard to the Takeover Directive. While national takeover regulation clearly is an important factor for member states' preferences regarding European takeover regulation, this project will not focus on any national context in a comprehensive way. Although it clearly is of great significance which Member States will decide

to implement the optional arrangements, this project is not concerned with ‘Europeanisation’ of corporate governance in the sense of how European regulation is influencing national corporate governance regimes and regulation (Cowles, Caporaso, and Risse 2001; Radaelli 2000) Thus, extensive national case studies will not be part of this research. Rather, I intend to use the examples of various countries’ approach to the Takeover Directive to locate transnational actors and to show the various interest constellations and struggles arising from the Directive.

Although the main focus in this research will be on management-shareholder relations with regard to the paradigm shift towards increased shareholder-decision making, the emergence of a market for corporate control and the transformation of corporate governance regulation in general has far-reaching consequences for various other stakeholders, most of all labour. A more thorough theorizing of the ‘stakeholder approach’, however, would mean going beyond the scope of this research – although the need for such an attempt is often acknowledged (Blair and Stout 1999; Tirole 2001). Rather, within the framework of the discussion of whether there is a power shift towards (certain) shareholders, the changing position and interests of stakeholders, and in particular labour/employees, will be taken into account as well. Since the EU is not operating in a political vacuum, and since the focus of this research is explicitly on the transnational dimension of corporate governance regulation, developments and events outside the EU also have to be acknowledged. Dewing and Russel, for instance, point out that ‘it is interesting to consider the influence of the US on the EU and vice versa on policy developments in accounting, auditing and corporate governance.’ (Dewing and Russell 2004: 291) However, the predominant focus of this project will remain on the European arena.

## **7 Theoretical framework**

Drawing on earlier sections of this research outline, I now intend to give a very rough outline of where to locate this research project theoretically. This I will do by, on the one hand, framing the research questions in the broader context of a shift towards increased marketisation of European corporate governance and, on the other hand, by clarifying some of the concepts that are key to this process. The underlying tenet of this framework is based on the perception that any corporate governance regime and the transformations pertaining to it are an expression of a political process, motivated by certain interests and most likely contested by others. As Susan Strange maintains, ‘these arrangements are not divinely ordained, nor are they fortuitous outcomes of blind chance. Rather, they are the results of human decisions taken in the context of man-made institutions and sets of self-set rules and customs’ (Strange 1988: 18 ).

With this in mind, it is crucial to reveal and analyse these political dimensions. The current transformation in corporate governance regulation, thus, as I will argue, represents a shift towards the commodification, that is, the marketisation of corporate control in the European Union.

## 7.1 The commodification of corporate control

Since in a functioning market for corporate control publicly listed companies are subjugated to the laws of this market, they themselves become a commodity (Windolf 1994: 81). If this is the case, as Polanyi argues, under the logic of the market, ‘no arrangement or behaviour should be allowed to exist that might prevent the actual functioning of the market mechanism on the lines of the commodity fiction’ (Polanyi 1957: 73). This, of course, has major consequences for the socio-economic configuration of any systems where the market for corporate control is established. Drawing on Polanyi, I intend to sketch to which extent the market for corporate control impacts on existing institutional and socio-economic arrangements, and in how far the logic of the takeover market is ultimately based on market-driven assumptions which aim at further disembedding the corporation from its societal context.

The perception of a company as a commodity which can be bought and sold is one of the underlying principles of this process – based on neoclassical economical assumptions of rational actors and the fundamental efficiency of the market. The basic mechanism of the market for corporate control is commonly assumed to be the chance ‘for the good to take over the bad’ (Bolkestein 2004). The evaluation of ‘good’ or ‘bad’ performance, in this respect, takes place on the grounds of shareholder value, i.e. the maximisation of share price and cash flow to the shareholders (Rappaport 1998). Any other objectives than the maximisation of shareholder value, as mentioned in the first part of this outline, are thus perceived as obstructing the proper functioning of the market. Rather, the market for corporate control is assumed to be an apolitical institution for buying and selling publicly listed companies. Interestingly, when looking at the actual process of corporate takeovers, it becomes apparent that they are far from being detached from social interaction (see f.ex. the PR battle during the Mannesmann Vodafone takeover (Höpner and Jackson 2001). Granovetter’s concept of the ‘embeddedness of economic action’ grasps this neglect very well by arguing that

Neoclassical economics are operating with an atomized, undersocialized conception of human action. [...] The theoretical arguments disallow by hypothesis any impact of social structure and social relations on production, distribution or consumption. (Granovetter 1985: 483)

Another aspect of this marketisation of corporate control is the redistributive consequence of a functioning market for corporate control. De Jong has shown that in a corporate governance regimes characterized by the absence of a market for corporate control, a higher share of net added value is being paid to employees and other stakeholders, while in comparison to this in corporate governance regimes which, like the Anglo-Saxon model, sustain a market for corporate control, about 3-4 times the share of net added value is being paid to shareholders (de Jong 1997: 18). This redistribution raises serious questions of in whose interest the emergence of corporate control would be, and which consequences it could have for other groups.

This also pertains to questions about both the form and the content of takeover regulation,

which can be seen as being increasingly market-oriented. The reliance on processes of benchmarking and finding a ‘best practice’ can be set within this context. The definition of what ‘best practice’ entails, however, is ultimately based on political decisions. What’s more, with the new Takeover Directive in force and other parallel developments granting far-reaching rights to companies to decide in which jurisdiction they want to incorporate,<sup>4</sup> this development is likely to lead to an increase in regulatory competition.

The basic idea of regulatory competition is that, in the long run, competition among corporate laws can be seen as a process of experimentation that leads to the emergence and selection of superior corporate laws (Heine and Kerber 2002: 61)

This, however, means that the role of public actors in the regulation of the market for corporate control is further eroded, since companies’ decision to be regulated under a specific jurisdiction is by no means subject to any democratic control, but merely based on market-driven principles.

## **7.2 Social forces in the making of corporate governance regulation in the EU**

The perpetuation of this market-oriented principle of corporate governance also requires an analysis of the role of various ‘experts’ in advancing it. With regard to this in the area of corporate governance, Dewing and Russell assert that

in contrast to auditing and accounting (subjects amenable to the application of private-sector professional and technical expertise), there is no equivalent international corporate governance ‘profession’ that has produced ‘ready made’ corporate governance ‘solutions’ (Dewing and Russell 2004: 300).

In contrast to this, I would argue that we are actually witnessing a development where corporate governance networks and ‘experts’ having an increasing influence on policy making and agenda setting. While the ‘solutions’ they offer are, of course, still highly contested, it is none the less essential to analyse their role in propagating and disseminating their ‘version’ of ‘good corporate governance’ in the context of the transformation of corporate governance in the EU (and, for that matter, on a wider scale, since these networks tend to have external links (mainly) to the US) (see f.ex. High Level Group of Company Experts 2002). Gramsci’s notion of the role of the ‘organic intellectuals’ will probably provide a useful heuristic here to show how these private and supposedly neutral ‘experts’ are not only instrumental in sustaining specific political choices, but are actually proactively contributing to the perpetuation of a market-driven corporate governance regime.

By focusing on the contested nature and the open-ended character of the transformation of corporate governance regulation rather than the mechanics of persistence, the actors and ‘social forces’ advancing and contesting these regulative transformations become important. These social forces are ‘located in the wider structure of the social relations of production, which *do not determine but shape* their interests and identities’ [emphasis in original] (Bieler and Morton

2001) By linking these forces to a concrete political project, the agenda behind specific political decisions and developments can be accounted for. The salience of identifying transnational agency in the process of the restructuring and transformation of European capitalism has been demonstrated in previous studies (see f.ex. van Apeldoorn 2002 on the European Roundtable of Industrialists) – however, to date there is no account of which transnational actors shape the processes of corporate governance regulation in the European Union, and which ideological underpinnings and political strategies motivate them.

With regard to the increased marketisation mentioned above, this has to be seen within the context of what Stephen Gill has characterised as ‘new constitutionalism’.

to separate economic policies from broad political accountability in order to make governments more responsive to the discipline of market forces and correspondingly less responsive to popular-democratic forces and processes [...] Central objectives in this discourse are security of property rights and investor freedoms, and market discipline on the state and on labour to secure credibility in the eyes of private investors, e.g. those in both the global currency and capital markets. (Gill 1998: 5)

This pertains also to the underlying ‘social purpose’ of the European integration project (van Apeldoorn 2002), and thus of corporate governance regulation as such. To contextualise corporate governance regulation as part of the broader context of the European integration project means that the fundamentally political dimension of these transformations can be exposed. While there have been first attempts at conceptualising corporate governance regulation along these lines (Bieling and Steinhilber 2002), there has not been a systemic analysis of in how far this contextualisation can help to answer the question of why the marketisation of corporate control is so ardently advanced, and why this regulation takes the form that it does. There is also an apparent need to move beyond the still somewhat state-centric analysis of the varieties of capitalism and corporate governance regimes in particular. This research project seeks to fill these gaps, and to help bring about a deeper understanding of the changes in corporate governance regulation.

Contrary to what Hansman and Kraakman argue (2001), ‘the history of company law’ and corporate governance is anything but over. Quite the opposite, with the ongoing politics around the transformation of corporate governance regulation, we are in for a whole lot more developments in the future. While this necessarily means writing on a moving target, the very excitement and significance of corporate governance regulation for socio-economic conditions are bound to make this project extremely interesting, to say the least.

## Notes

<sup>1</sup> For a detailed overview on anti-takeover defences, see Shleifer and Vishny, 'A survey of Corporate Governance' Shleifer, A. and R. W. Vishny (1996). *A Survey of Corporate Governance*. NBER Working Papers. Cambridge

<sup>2</sup> Already in 1965, Andrew Shonfield had observed the alternative structures of modern capitalism Andrew Shonfield (1965), *Modern Capitalism: The Changing Balance of Public and Private Power* Oxford UP

<sup>3</sup> Companies in member states with structural barriers to takeovers (f.ex. voting caps, multiple voting rights) would still have means to obstruct or frustrate a takeover.

<sup>4</sup> See f.ex. the the Centros and Überseering decisions of the ECJ (for a good overview on regulatory developments in company law in general see (Heine and Kerber 2002).

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