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« UNIFICATION OF CORPORATE LEGISLATION: WORLD TRENDS, EU LEGISLATION AND RUSSIA'S OUTLOOK »

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Unification of Corporate Legislation: World Trends, EU Legislation And Russia's Outlook[1]

Content

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Chapter 1 Reception and unification of corporate legislation: the world process and national restrictions

1.1. Reception, convergence and unification

First of all, it is necessary to take into consideration the natural process of reception and unification of law which may be going on at the national, regional and international levels.[2]

At the national level, development of the corporate legislation cannot be assessed adequately unless the influence of the rules of other countries is taken into account. Latest developments in the area of corporate law are quickly borrowed by legislation and practice of other countries, which means that "corporate law in every country is developed by the international effort" (Ripert, p. 678). However, unification is not the result of international agreements but mostly of unilateral reception of concepts, constructs and institutions of foreign corporate law. Most of the lawyers consider such an approximation of legal systems not as unification but as copying or imitation of foreign law (Matteucci, p. 338).

Historically, on the basis of the available evidence, most far-reaching effect on evolution of corporate legal regulation is produced by the laws of France, the USA and Germany. The general importance of the Civil (1804) and Commercial (1807) Codes by Napoleon and the Commercial Code (1897) by Bismarck do not require any comment. Reception of the German civil law by Japan in the second half of the XIX century was brought about by the necessity to regenerate the legal regulation of the economic activities in the situation where the country's own legal material was missing. The 1951 Japanese Law on Corporations, for the most part, was a duplicate of the US corporate legislation. Convertible debentures – statutory instruments in most European countries – were initially introduced in the USA. The German Law dated 29 April 1892 was the first to introduce "public limited-liability partnerships" which later became a standard legal and organizational form of small and medium-sized businesses worldwide. In their turn, the law on public limited-liability partnerships adopted by many European countries produces their effect on the legal status of private companies in England and close corporations in the USA.

Reception is characteristic of the current period, in particular, of the 90s in the last century, when the economic legislation of transitional economies was undergoing a dramatic transformation (see below).

Under the present circumstances (at the turn of the century) it would be proper to discuss **convergence** – approximation of national models of corporate governance (Table 1) through mutually beneficial exchange of certain elements (within the framework of reception).

In the last quarter of the century, for all the countries across the world, contraction of the authority of the general meeting of shareholders and emergence of the Board of Directors (the Board) as an independent body is the most common and characteristic trend in the development of elements of the management structure. Now, to the contrary, a discussion about development of such a form as "virtual shareholders' meeting" is gaining momentum, which has become possible due to the progress in new technologies. In particular, the issue is on the agenda of the EU High Level Group of Company Law Experts set up in 2001.

[2] For more detail see: Kulagin, 1997, pp. 66-71, 213-219.

Table 1. Comparative characteristics of the "English-American", "Japanese" and "German" models of corporate governance

	English-American*	Japanese	German **
General characteristic and specific features	- Large number of non-affiliated shareholders; - Property dispersion; - Preference for share financing	- High share of affiliated companies among the shareholders; - Cross-holdings "keiretsu" (groups of companies united by joint ownership and management); - Informal ownership concentration	- Long-term interest of banks in corporations; - Long-term investment of corporations in other non-affiliated corporations; - Formal ownership concentration (family control through majority interest); - Preference for bank financing
Important issues:			
(1) Key players	- Managers; - Directors; - Shareholders Principle of relationship: "balance of forces "	- Main bank-creditor and the core of "keiretsu" (informal control by managers); - Affiliated company-shareholder of the corporation; - Managers; - Government Principle of relationship - "establishing ties"	- Commercial banks (shareholders and creditors); - Corporate shareholders Principle of relationship - "direct control " (objectively) and "social partnership" (formally)
(2) Key shareholders	Growing share of non-bank financial institutions and corporations; High share of individual shareholders; Low share of foreign investors	Growing share of banks, insurance companies and corporations	Growing share of banks, pension funds and corporations; Low share of individual shareholders; High share of foreign investors
(3) Board membership	Unitary board includes independent directors (a trend to increase their numbers on the board)	Board of executive directors comprises affiliated persons (executive directors, department heads) as well as retired officials. "Outsiders" are rarely represented.	Two-chamber management structure: - executive body (board – corporation officials) - supervisory board ("independent affiliated shareholders and employees)
(4) Legal and institutional framework	USA: laws of the states – rights and responsibilities of corporations, SEC - "corporation - shareholder" and "shareholder-to-shareholder" relationship; UK – Parliament and	Ministries in charge of the industrial policy; Securities Department of the Ministry of Finance and Stock Exchange Committee (copying of the US legal regulation in the post-war period)	Federal level: laws on corporations, stock exchanges, groups; commercial law, PLC management rules; "Lands": stock exchange regulation

	Securities and Investment Board		
(5) Information disclosure requirements	Well-developed, rigid and detailed legislation; Financial information is provided quarterly; information on personal bonuses, data on all shareholders having over 5% of the shares; stock exchange plays an important role	Less rigid requirements; financial information is provided half-yearly; aggregate information on bonuses; information on 10 top shareholders	Less rigid requirements; financial information is supplied half-yearly; aggregate information on bonuses; information on all shareholders having over 25% of the shares; information on supervisory board members and the number of shares they have is not provided
(6) Mechanism of interaction between the players	Overall: on the basis of a division between ownership and management (control) Technically: a simple and apprehensible mechanism, shareholders get information about the shareholders' meeting, the annual report and ballot papers by post, vote by proxy	Overall: weak influence of independent (non-affiliated) shareholders on corporation's affairs due to a specific mix of the shareholders, problems with voting by non-Japanese shareholders and institutional investors Technically: a simple mechanism, all the shareholders have access to annual reports., materials of the shareholders' meetings, vote by proxy	Overall: division between control and management (two-chamber board) Voting incapacity legally authorized (number of votes can be less than the shares number). Procedures of considering proposals by shareholders are well-developed (to satisfy small shareholders). Obstacles: - most of the shares are not registered (share to bearer), that is why the documents are sent first to the depository bank to be forwarded then to shareholders; - it is necessary to be present at the shareholders' meeting or to be represented by the depository
(7) Corporation's actions that require an approval by the shareholders	(Mandatory) – Election of directors and appointment of auditors as well as option plans, reorganization, merger and buying out a controlling block of stock. The right to introduce business proposals. In the UK – the dividend size.	(Normally) –Payment of dividends, funds distribution, election of board members and appointment of the auditor; changes in the capital and the statutes, severance pays to directors and auditors. The upper limit to bonuses for directors and auditors. From 1981 – the right to introduce business	(Normally) – Payment of dividends, funds distribution, election of the supervisory board members and appointment of the auditor, ratification of decisions by the executive and supervisory boards over the financial year; changes in the capital and the statutes, mergers, the upper

		proposals (Commercial Code), which is not encouraged	limit to bonuses. The right to introduce business proposals is widespread.

** In contrast to the purely American and purely English models, the English-American model is adopted by Australia, Canada and the Netherlands.*
*** The German model (certain elements) is applied in Austria, the Netherlands, in Scandinavia and in some French and Belgian corporations. Most of the European transitional economies also prefer this model.*
Sources: Sherman, Babcock, Mazullo, 1994; Berglof, 1990; Prentice, Holland, 1993; Monks, Minow, 1995; Turnbull, 1997; Charkham, Simpson, 1999; Charkham, 1994; Board Directors…,1992; De Vroey, 1973; Morin, 1988; Roe, 1994; Wouters, 1973.

Some researchers point to the emerging convergence of the models and some of the characteristics (apart from the decline and the potential revival of the role played by shareholders' meetings).[3] In the USA, for example, this is evidenced by the increasingly strong pressure on the part of the investor "vote" (alongside the growing share of institutional investors). In the 80s, in Japan, a certain loosening of ties within "keiretsu" between banks and strong corporations capable of obtaining finance on the international market. Opponents to the American model insist on the necessity to give more power to the "vote". At the same time, opponents to the German and Japanese models advocate making them more open, flexible, easier "to go into" and "to go out". Thus, the situation justifies a discussion about the trends and unification of the main components of the securities market infrastructure.

The gradual change in understanding the outlook for and significance of various external mechanisms of corporate governance is also very important. Capital market and corporate governance market are important by definition. According to some estimates tomorrow is not with the institutional but with the market control. The experience of Germany, where capital markets are being quickly developed alongside intensification of processes of public takeovers is evidence to that. Moreover, the delay in adopting Thirteenth Directive on Takeover Bids by the EU Council made Germany to develop its own national act on takeovers irrespective of the outlook for adoption of the Directive.

Such mechanisms as audit and information disclosure (key elements in the English-American model) are viewed in Germany as the foundation of the future corporate governance (the 1998 Act), while the USA academe increasingly deny them any such role. Among the arguments for the rejection one might point to the hypothesis of effective capital markets, lack of confidence in regulation and regulation agencies (including the SEC), some elements of the terminology of the social choice theory, etc. (Hopt, 2000). The 2001 "Enron" scandal might become a strong argument for this position.

Nevertheless, in general, it is possible to identify some world-wide trends characteristic of further corporate law improvement:

- stronger demand for "transparency" (information disclosure) of PLCs activities;
- parallel process of widening the rights of PLCs management bodies and increasing shareholders' control over them;
- tougher judicial control over PLCs activities;
- development of legislation on protection of the rights of small shareholders across the full range of issues (priority of buying newly issued shares, qualified majority, merger and takeover rules, cumulative vote, etc..);

[3] For more detail see: Gray, Hanson, 1994.

- development of legislation on protection of the rights of PLCs' creditors;
- tougher rules on issuing shares, changing the authorized capital, introduction of the rule of inadmissibility of increasing profit at the expense of the fixed capital;
- approximation of the legal status of a share and a debenture;
- focus on issues concerning PLCs' reorganization, transformation of PLCs into other types of association and vice versa;
- tougher regulation of relationship between various legally independent but economically interfacing PLCs (for example, the notion of "group" in the French law).

The above short list of issues demonstrates that they are not less important for many transitional economies (including Russia) where the relevant transformation has reached a certain qualitative level.

The attempts to develop a certain standard of "the XXI century corporation" related to the ever increasing economic globalization and emergence of a new economy based on information and telecommunication technologies produce their direct effect on the issues under discussion (see Yudanov, 2001). Objectively, the driving forces behind the current corporate governance reform across the world are:

- internationalization and competition;
- quick growth of the number of shareholders and changes in their structure;
- emergence of new industries;
- development of financial markets and new technologies.*

The large number of various national and international codes of corporate governance that came into being in the 90s reflects the trend and increasingly affect the conventional legislation (Hopt, 2000; Gregory, 2001).

At the same time the view that efficiency of running "the XXI century corporation" will increase if the principles of national entrepreneurship are taken into account is quite widespread. As E. Berglof and E.L. von Thadden observed, generalization is more often harmful than useful and all the international codes should acknowledge cross-national differences (Berglöf, von Thadden, 1999). Attempts to transplant institutions (imitation of import of institutions) based on political and ideological considerations and not taking into account national traditions and economic and legal peculiarities usually fail.

Within the EU this process is related, first of all, to the objectively remaining cross-national differences in forms and methods of corporations' activities. The British model is traditionally linked with the market approach. The "Rhine Capitalism" model that envisages financing at the expense of strategic partners (banks, insurance companies) has not lost its importance for Germany. Resources of oligarchic financial groups and leading financial-industrial corporations respectively dominate in Italy and in Spain. Quite often, the state plays the role of the most important creditor in France. In Scandinavia, the "welfare state" directly implies a strong state influence. From the point of view of corporations' operations, one common element – the lack of any significant financing through the stock market (i.e. through intermediaries) and the dominance by strategic partners – acquires a principle importance.[4]

[4] It should be noted that as far as the European export and import (and the scale of integration into the world economy) are concerned the two countries that are the main protagonists of the "corporate capitalism" within the EU – the UK and the Netherlands – hold the leading positions. (See Yudanov, 2001).

At the international level, the discussions have intensified about the wisdom of other countries, the EU Member States included, accepting a single (mostly American) model.

Within this discussion the attention is focused on general principles of activities of a modern large corporation "the XXI century corporation" that are often equaled with the "American" approach and attempts to impose the English-American business model on the rest of the world. In principle, the "one size does not fit all" approach can be accepted, but responsibility, accountability, fairness (legalism) and transparency are real universal standards for every regime of corporate governance (Fremond, Capaul, 2002).

More specific elements of various models are hardly transferable. As an example, E. Berglof and E.L. von Thadden take the 1993 EU Directive on Transparency concerning ownership and control, i.e. the areas where the continental EU countries are lacking an effective regulation. Its adoption had been prompted by the bitter criticism of the corporate governance by the proponents of the market approach which considers transparency of information on ownership and control systems to be inherently positive. However there is evidence that the Directive did not result in any tangible progress: most of the companies, even those in the EU countries, have found means of by-passing the limitations set by the EU (ECGN, 1998). A similar situation is emerging in Russia as regards the use of the "English-American" mechanism of protecting the rights of minority shareholders under the condition of growing corporate ownership concentration.

At the same time, the new economic and technological realities have presented big EU corporations with the issue of supplementing the finance provided by the strategic partners with resources of the national and international capital markets. The policy of "inflating corporate property» is pursued by "Siemens" of Germany, "Alkatel" and "Danon" of France, "Telephonica" of Spain, and others. [5] Nevertheless, serious obstacles to borrowing the American approach remain. They are:

- dogmatic orientation to the share growth (company's activities in the interests of the shareholders only) is checked in the EU countries by the dominating principle of "social responsibility of the companies";
- comparative predominance of long-term strategies and motivations in European companies' activities is also a factor of the cautious attitude towards "shareholder dictatorship" that might require a maximum efficiency in the short term to secure market value growth;
- high-level transparency of the corporation typical of the "corporate capitalism" is not always characteristic of the principles of the European business culture;
- existing doubts about stability of the "new economy" and some European analysts' belief that the high level of development of the American stock market is only transitory (Yudanov, 2001, p.70).

Approaches to reforming the company law also differ significantly and recommendations bear the marks of the social status of their authors (Hopt, 2000):

- reform of the Board of Directors;
- more active role played by private and institutional investors (as a reaction to the globalization of markets and modern technologies);
- development of laws and rules governing activities of "company groups" (first of all, by judges and regulators in some countries of the continental Europe);

[5] "The Economist" (2000, May 20, pp. 31-32) writes that although the total number of shareholders in the continental Europe remains insignificant they gradually outnumber civil servants in France, union members in Germany and unemployed in Italy.

- cooperation with the hired labour "at the shop-floor and the Board of Directors levels";
- protection of the rights of shareholders and investors as an absolute priority in the interests of economic growth and transformations; priority of the market over inflexible national laws and doctrines (representatives of the modern economics).

When studying the processes of **unification** of the law at the regional and international levels the term "internationalization of the law" is sometimes used to denote the process. In legal literature and in the texts of international agreements the process of establishing a uniform legal regulation or the results of this process are usually named approximation, harmonization, or coordination of the law.

In 1999, OECD made an attempt to establish certain uniform principles of corporate government as a recommended set of best practice standards (OECD, 1999).

Nevertheless, the EU experience gives the fullest (world-wise) understanding of the process taking place at the level of one of the best developed regions of the world. Importantly, the decisions by the EU increasingly affect the civil and commercial law of the Member States and, if the candidate countries are taken into account, of the entire European region.

Researches point to the fact that the limits of the EU legislation affecting national corporate rules are sometimes hard to identify (Dine, 1998). This happens because most of the changes brought about by the EU acquire the status of legislation through standard law-making procedures. Many people do not understand that a huge number of changes in the legislation come about due to the Directives i.e. they have been included into the list of measures aimed to reform the corporate legislation as the EU Member States bear responsibility for implementing the Directives.

In 2001, the issue of taking into account the EU uniform rules when improving the Russian model of corporate governance acquired a special importance.[6] It is well-known that the necessity of establishing a free trade area between the EU and Russia (including creation of conditions "for realization of freedom of establishment" and "movement of capital") was stressed by the Partnership and Cooperation Agreement signed in Corfu on June 24, 1994 that came into force on December 1, 1997. The EU Collective Strategy on Russia (June 3-4, 1999) has as its objective "integration of Russia into the common European economic and social space". The strategy envisages establishing in future "a free trade zone between Russia and the EU" and, as the legislations and standards approximate gradually, a single economic space.

In May 2001, at the Russia-EU summit an idea was put forward of advisability of establishing a "Common European Economic Area". To some extent, the 2010 Strategic Programme aims to adapt the European institutions (criteria) to the Russian conditions which implies, in particular, actions in such areas as effective work of the competition mechanism, legislation stability, property protection, effective bankruptcy procedures, financial market stability, adequate state and administrative institutions.

When making an assessment of the outlook for approximation of the Russian and European standards on corporate governance it is necessary to take into consideration both the EU experience as such and the specificity of development of company law (corporate governance models) in the transitional economies.

[6] For more detail see: Borko, 2001; Gorsky, 1998; Zsurkin, Kudrov, 1996; Leshukov, 1998; May, 2002, pp.18-20; Fonten, 1994; Shmelev, 2002.

1.2. Some problems with the traditional models

To a significant extent the mechanism of corporate government define the peculiar characteristics of economic and legal structure within which shareholders can realize their property rights and the way corporate ownership is distributed. At the same time, lack or relatively limited presence of one type of mechanisms (related, for example to the market-based change of corporate control) can be offset by the presence of others (such as ownership of large blocks of shares, family control, membership in a well-established group or a special role played by the head bank). Intensification of competition on the markets of goods, capital and labour invariably emerged as the necessary prerequisite for improving efficiency of corporate control.

It appears that each of the known types of corporate governance has its strong and week sides. Citing the experience of the 50-s - 70-s (when Japan and Germany demonstrated high rates of economic growth) many authors stress the importance of corporate governance that relies on the largest banks. Recently, however, it has been increasingly often noted that this type of corporate governance can provide an excessively strong protection of ineffective companies and, what is more important, is characterized by a somewhat stronger force of inertia and by less susceptibility to radical technical and economic innovations. At the same time, more attention is paid to the role played by flexible market mechanisms and their disciplinary functions. Many of the conclusions of this type are the result of application of interesting theoretical models and empiric studies (see, for example, Morck, Nakamura 1999).

At the same time, it is hardly wise to overestimate the role of differences between the above types of corporate governance. S. Kaplan, who wrote a number of papers on differences in corporate governance between various countries, came to the following conclusions. Normally, the possibility of removing top managers from office increases with considerable deterioration of the corporation's positions. Of particular interest are the results of the following calculations: the values of foregone earnings elasticity of top managers turnover and drops in market share prices (for the relevant corporations in all the three countries) elasticity are apparently values of the same order (Kaplan, 1997). In other words, judging by the above evaluations the effects produced by different mechanisms of corporate governance and manifested in the intensity of the turnover of top managers happen to be rather similar.

It would be an illusion to believe that under the conditions of a developed economy – irrespective of the by-country differences – all the problems of corporate governance have been resolved. Forming a specific model is a permanent process of conceptual and narrow-subject discussions, of bringing out new and new offences against the law, of adequately improving the mechanisms of internal and external controls in the corporation, of providing the legal framework and protection of investor rights. Realities of the economic development also affect the practices of corporate governance. [7]

It should be noted that none of these models is perfect. Both the German and the Japanese models draw criticism for being "to closed and too shielding managers too much" (Gray, Hanson, 1994). In Germany criticism is increasingly leveled at the banks carrying out exclusive operations on the stock market and holding large blocks of shares of corporations for damaging the interests of the depositors. At the same time there is an obvious conflict: (a) between the interests of banks as credit organizations and their interests as strategic investors; (b) between the interests of banks as strategic investors and the interests of small shareholders-financial investors. Predominance of bearer shares

[7] One of the most demonstrative examples of the 90-s – the discussion in the USA about repealing the Glass-Steagall law that separated commercial and investment banks after the Great Depression of the 30-s. At present, the abolition of rigid restrictions makes more urgent the issue of the role banks play in corporate governance (in the USA included).

is an obstacle to effective realization by shareholders (foreign shareholders, in particular) of their rights.

The Japanese system of affiliated shareholders in fact discredits the rights of "independent" shareholders. Additional problems of portfolio investors in Japan are caused by the practice of holding all the shareholders' meetings at the same time, by the negative attitude towards the shareholders' initiative (proposals).

At the theory level, as far as the English-American model is concerned it is customary to assume that dispersion of ownership results in the shareholders becoming passive (which is particularly characteristic of large companies with greater numbers of shareholders, a clear-cut separation of ownership and control, and higher costs of industrial actions). The takeovers market viewed within the American model as the most important tool of corporate control draws criticism for its potential to destabilize the situation in the companies affected. The conventional criticism of the American model is focused on the passive behaviour of outsiders-members of the Board of Directors. It is assumed that the trend shall further develop. One more trend characteristic of the USA is concentration of corporate affairs in the hands of a narrow group of persons i.e. managers.

There is also a long list of issues of practical and legal nature that have been and remain the subject of discussion. Here are some of them:

- to what extent the degree of ownership (control) concentration affects relationship between the shareholders and corporations' performance;
- what is the relationship between the functions of the Board of Directors, the distribution of shareholders' membership in the Board of Directors, and the actual distribution of ownership (shares) within corporations; [8]
- to what extent Boards of Directors should be accountable to the shareholders, what incentives they have to represent the interests of the shareholders effectively, what is the measure of their responsibility for developing (adopting) corporate strategy;
- what is the optimum ratio of "internal executive" directors to "independent" directors in the Board, how to ensure adequate efficiency of independent directors and delineate reasonable boundaries for their interference;
- where lies the divide between corporate governance and management, between managers' accountability to the Board of Directors and the Board's interference into their day-to-day activities; [9]
- what should be the solution (is it needed at all?) to the "free rider" or the "sleeping partner" problem i.e. the situation where every small shareholder in a big corporation seeks to shift his responsibility for control over managers to the other shareholders;
- contrariwise, how to secure effectively the rights of small shareholders without permitting them to behave in a destabilizing way;
- whose interests (the shareholders', all the financial investors, all the "partners" in the corporation) should the Board of Directors represent, what costs are involved, who should bear the costs, how to distribute the costs between the various groups of the "partners" ?

[8] This is of principle importance as the characters of Boards of Directors "controlled" by a host of small shareholders and those in corporations under unambiguous control of one or more large shareholders differ significantly. In the former case the role of the Board is much more important.

[9] One of the individual but important questions here is the one how detailed should be a contract between the corporation and the hired managers. On the one hand a detailed contract is necessary for control, on the other no contract can provide for every eventuality.

- should the interests of small and large shareholders, of owners of ordinary and preference shares be represented separately ?

The above list of the current problems alone makes it possible to state that in a certain sense a corporation is a potential mix of various conflicts of interests:

- conflict of interests of shareholders and managers ("profits" - "wages", "savings" – "prestige", "portfolio investment" – "permanent job", "high profits" – "being prepared for all eventualities", etc., correspondingly);
- personal conflict of interests of the Board directors and managers (by virtue of the residual principle of the executive directors' authority);
- conflict of interests (in the English-American model) arising when the positions of Chairman of the Board of Directors and Director General (Executive Director) of the corporation are held by the same person;
- conflict of interests between various groups of shareholders depending on the aims: short-term or long-term profits, security and secure long-term investment, strategic control and financial investment;
- conflict of interests between various groups of shareholders depending on the size of the block of shares (actions by large shareholders to the detriment of the interests of small shareholders, up to ownership redistribution);
- the latter conflict potentially manifests itself in the "shareholders (group of shareholders) – Board of Directors" conflict (depending on what type of shareholders have their interests represented by the Board of Directors);
- conflict of interests between the shareholders and owners of the corporation's debentures ("maximization of the residual profits" - "fixed yield on borrowed capital", "high propensity to risk" - "conservative line of behaviour", "all the earnings from risky operations" - "major losses from bad investment");
- similar conflict of interests between shareholders and other financial investors providing borrowed capital (banks, etc.).

Resolving or at least mitigation of the conflicts can be viewed as one of the main objectives of reforming corporate governance alongside the general aim of protecting the shareholders' interests.

Thus, even in the countries having stable models of corporate governance there are many problems complicating the institutional and legal framework of corporations' activities. In one way or another, all of them are of utmost importance for the models emerging in the transitional economies.

Chapter 2. Specific features of company law unification within the EU

2.1. General

The Treaty of Rome on establishing the European Community signed on March 27, 1957 envisages creation of a common market of goods, capital, labour and services. One of the areas of the

activities of the Community was defined as "the approximation of the laws of Member States to the extent required for the functioning of the common market" (Article 3(h)). [10]

The scope of the Treaty of Rome was widened by signing in 1986 the Single European Act (SEA). The SEA introduced a number of important changes in the procedure. In particular, it allowed the Ministerial Council to pass decisions by majority vote. The text of the Treaty of Rome with the changes introduced by the SEA was considerably altered and amended with signing of the Maastricht Treaty on November 1, 1993.[11]

As far as corporate law is concerned the problem lies in the fact that the interested parties themselves (companies) fall under the jurisdiction of different national legal systems. Consequently, complex legal "safeguards" have to be incorporated into the contracts they sign. The contracts shall be written taking into account legal rules prescribes by different national law systems. This is why the EU attempts to harmonize a number of corporate legal rules.

One more problem is related to the fact that harmonization of the corporate law aims to realize fully the freedom of establishing undertakings which in its turn helps avoid market distortions. However, the EU Member States having a well-developed legislation in the area will find themselves disadvantaged. Until at least a minimum level of harmonization is achieved there is a danger of producing the "Delaware effect", i.e. companied will prefer to be incorporated in the EU Member State having the most liberal corporate law.

It is obvious also that harmonization of company law is closely related to the entire set of measures in the area of company regulation. In particular, one of the serious obstacles is the abortive attempts to harmonize tax regimes although some progress has been made in the area recently. [12]

Three types of law unification within the EU are envisaged:

1) uniform rules in the text of the Treaty of Rome (for example, Articles. 85-87 on banning agreements, associations, etc. hampering freedom of competition and on prevention of abuse of dominant position on the market) that directly apply to all natural persons and legal entities and have priority over national rules;

2) law harmonization through signing international conventions (Article 220) that become an integral part of the Treaty of Rome (for example, the Convention on Mutual Recognition of Partnerships dated February 29, 1968);

3) Article 189 of the EU Treaty establishes a number of procedures of the Council and Commission legislative work resulting in adoption of documents known in general as "acts". First of all we refer to the right of the EU governing bodies (the Council and the Commission) to issue special types of acts: regulations and Directives.

Apart from regulations and Directives the acts include decisions are addressed to the Member States and natural persons and are binding for them, recommendations and opinions. The latter are have no binding force but induce certain actions.

[10] Hereinafter the overview of the relevant EU legal rules is based on the following sources: the EU official publications (OJ) and sites: (http://europa.eu.int/comm/internal_market/en/company and EUR-Lex Community Legislation, as well as: Asoskov, 1998; Kulagin, 1997; Shelenkov, 1998; Bermann et al., 1997; Buxbaum, Hopt, 1988; Dine, 1998, pp. 321-349; Evans, 1998; Wooldridge, 1991; Dorresteijn et al., 1994; Favret, 1996; Zaphirien, 1970.

[11] One of the basic changes was the European Community acquiring the name of the European Union. However, it is important to note that the term "European Union" was not substituted for the term "European Community". While former term is used as a collective name for the governments of the Community Member States, the institutions of the Community retain their prerogative to initiate and enforce legislation.

[12] Council Directive of June 23, 1990 "The Common System of Taxation Guidelines in the Case of a Parent Company and Subsidiaries of Different Member States" and Council Directive 91/308 EEC (OJ 1991 L166/77).

Regulations (rules of procedure) have direct application in each of the Member States (Article 189, p. 2). No national legislation is required to implement them. However, certain legal framework might be needed to "transform" its results into the notions well-understood at the national level and to fill-in lacunas in the legislations.

For researchers the Directives are a source of "Community law" as an autonomous legal system operating in parallel with national systems and the international common law. Directives (which are in fact laws adopted by the EU Council) are binding, as to the result to be achieved, upon each Member State to which it is addressed, but leaves to the national authorities the choice of form and methods (Article 189, p. 3).

It should be noted that according to the rulings by the European Court many of the Directives are of "direct" action (characterized by direct action or enforcement in relation to national laws of the Member States) and have precedence of over national laws in case of disagreements between them.[13] For example, the ruling reached in the cases C-19 и C-20/90 Karella v. Minister of Industry, Energy and Technology (1991 OJ C166/12) proclaimed that certain provisions of the Second Council Directive on corporate law have direct action. It is possible also that in case of non-observance of a Directive by the Member State a natural person can initiate against it a case that might result in compensation payments (see cases C-6 и 9/96 Frankovich and Bonifaci v. Italian Republic ([1992] ECR 133).

Directives can concern almost every section of commercial law although formally they are adopted to harmonize legislation or to remove differences between national acts violating the competition rules.

Member States shall coordinate their legislation with the Directives' provisions. Typically, this is done through passing special laws. For example, in the UK, Directives adopted by the Council become part of the British legislation through their practical application. In happens when the relevant ministry (in this case it is almost invariably the Ministry of Trade and Industry) develops an act that transforms provisions of the Directive into British terms. The act is then sent to the Parliament using the standard procedure. However, as the UK should enforce the Directive, the scale of legislative amendments is restricted.

In France, provisions of Second, Fourth, and Seventh Council Directives were introduced into the effective law by special laws and taken into account when adopting new ones. For example, the draft First Council Directive was taken into consideration when developing the Law on Commercial Partnership of 1966. In 1972, England adopted the Law on European Communities incorporating provisions of the relevant international treaties and acts of direct action into the country's own legislation. Section IX of the Law brought the British company law in line with the First Council Directive on public liability companies. As a result, the "ultra vires" doctrine in its conventional meaning (fixation of the principle of special legal competence of companies) was thrown aside. Taking into account the Second Council Directive, the British Law on Companies set the value of minimum fixed capital of a public limited-liability company at £ 50 000, envisaged that at least ¼ of the shares should be paid at the subscription time, etc.

In spite of the considerable progress so far, researchers note that harmonization by means of Directives cannot provide a complete and universal statute book and an absolutely "level playing field".

In order to ensure the harmonization effect (when implementation of the Directives will result in narrowing down the differences in legal rules to minimum), a Directive should be detailed and

[13] See, for example, Glotova, 1999.

inflexible. At the same time, excessive attention to detail increases the burden of regulation and inflexibility causes "fossilization" of the corporate law. Detailed rules might produce the "blocking" effect as the procedures of introducing changes into an adopted Directive are cumbersome and therefore the risks of the laws coming into collision with business practices are high. Despite a;; the details that the Directives contain the corporate regimes in the EU Member States still differ significantly.

The intensive interpenetration of the national laws and the EU legislation intensified by implementation of the Council Directives complicates considerably interpretation of legal acts. A European rule does not become integrated into national laws of the Member States through its systematic interpretation; the interpretation takes place outside the context of national regulation. Moreover, when this happens it is necessary to take into consideration provisions of the basic EU Treaties that establish primacy of the EU law over national legislations. Therefore it would be useful to avoid interpretations that divert national laws from the developing principles of the European private law. It is advisable to establish such a procedure of rule-making that would promote making decisions consistent with the general European law culture and, at the same time, eliminated restrictions unacceptable for other law systems (Zekker, 2001).

Overall, harmonization of company laws, rules of accounting and audit is considered as the most important area of establishing a single market of financial services and goods. Harmonization of the company law aims to attain the following key objectives:

- to ensure equal protection for shareholders and all the other persons (parties) related to a company;
- to ensure freedom of establishing an undertaking within the EU and promotion of international cooperation between companies of the EU Member States;
- to stimulate discussions of company law and corporate governance reform.

2.2. Directives concerning company law

First Council Directive (68/151 of 9 March 1968[14]) deals with issues that require immediate unification:

- the minimum list of documents and information on company activities to be provided for the shareholders and the public (he EU Member States should take measures to ensure compulsory disclosure by companies of the following information: the charter, the names of the company directors, the amount of the capital subscribed, the balance sheet and the profit and loss account, the winding up of the company, the appointment of liquidators);
- effectiveness of the obligations taken on by the company organs (for contracts signed before the company acquired legal personality the founders should without limit be jointly and severally liable while the PLC should be liable after approval of the contracts by the general meeting of its share holders). The Directive also fixes presumption of fairness: if the third party entering into contract with the company believes that the act is within the objects of the company the contract is considered as effective.
- control over company formation and nullity. Nullity should entail the winding up of the company but should not of itself affect the validity of any commitments entered earlier.

[14] OJ 1968 spec. ed. 41-45.

- Public limited partnerships are also covered by the Directive. Establishing the single EU system of information disclosure is the most important result of the implementation of the Directive by all the EU Member States.

Second Council Directive (76/91 of 13 December 1976[15]) concerns the harmonization rules that regulate the formation of public limited liability companies and maintenance, increase or reduction of their capital. Companies are obliged to disclose the following information: the type and name of the company, the objects of the companies, the place of registration, the amount of the subscribed capital, the classes of the shares, the structure and authority of the company's organs. The minimum amount of the subscribed capital of a public limited liability company should be not less than 25 000 ECU. If shares are issued for a consideration other than cash its valuation should be done by independent experts. The subscribed capital should be formed only by assets capable of economic assessment while undertakings to perform work or supply services should not form part of these assets. The Directive sets some other rules concerning maintenance of the capital. Shares cannot be issued without declaring their nominal value. Rules were set for companies acquiring their own shares. The general meeting of shareholders can delegate the right to increase the subscribed capital to another body empowered to do so for a maximum period of five years. Besides, the Directive gives the shareholders the right buy shares on a pre-emptive basis. The Directive has been implemented by all the EU Member States.[16]

Interpretation of the Second Council Directive was studied by the European Court which ruled that Articles 5 and 29 concerning an increase in the capital are provisions of direct action for legislations of all the EU Member States and are applicable not only in the situations of normal functioning of the company but also when it becomes subject to restructuring operations.[17] Obviously the decisions aimed to prevent placing newly issued shares without taking into consideration the rights of the shareholders and increasing of the subscribed capital before the scheme of the increase is discussed by the general meeting. Some experts hold an opinion that from the point of view of corporate law the value of the rulings is doubtful as they are based, for the most part, on the concept of "corporate democracy" that apparently is fortified through "saving of companies having certain social and economic importance (Dine, 1998).

Third Council Directive (78/855 of 9 November 1978 года[18]) regulates mergers of public limited liability companies. Two possible methods are envisaged: "merger by acquisition" (the operation whereby all the assets and liabilities of the company being acquired are transferred to the acquiring company) and "merger by the formation of a new company" (the operation whereby several companies are wound up without going into liquidation and transfer to a company they set up all their assets and liabilities). The shareholders are entitled to get equivalent stakes in the company formed as a result of the merger. The necessary valuations should be performed by an independent expert.

To protect the rights of the shareholders and creditors a merger shall be announced, in due time, by each of the merging companies; each class of the shares issued by the companies should be approved at a general meeting. Protection of the rights of employees should be regulated in accordance with Directive 77/187 as part of the EU legislation on social security and employment.

[15] OJ 1977 L 26/1.
[16] The Directive concerns public companies. However, some countries (Belgium, Netherlands) extended it to cover close companies which brings about differences in national regulations (Dorresteijn et al., 1994, p. 46).
[17] Karella v. Minister for Industry and the Organization for the Restructuring of Enterprises (1991 OJ C166/12, judgement of 30 May 1991) and Syndesmos EEC, Vasco et al v. Greec et al (ECR 1-2111, judgement of 24 March 1992).
[18] OJ 1978 L 295/36.

Fourth Council Directive (78/660 of 25 July 1978[19]) regulates drawing up of annual accounts of PLCs and limited liability partnerships. It comprises detailed rules of keeping accounts by companies divided into 3 types (large, medium-sized and small). Changes and amendments have been introduced in this Directive and Seventh Directive to ease the situation for small companies but including partnerships that fall under the provisions of the said Directives.[20] The Directive has been implemented by all the EU Member States although there is a growing doubt about the concept of "true and fair view" having the same meaning in all the countries.

Sixth Council Directive (82/891 of 17 December 1982[21]) concerns the division of public limited liability companies. The EU Member States are not obliged to implement this form of restructuring. However, if they use it the process should be in line with the provisions of the Directive. The company should wind up without going into liquidation. Allocation of the assets and liabilities to be transferred to each of the recipient companies should be subject to specific rules aimed to protect the rights of the shareholders and creditors. In case of any growth of the company capital the shareholders should have the right to buy shares on a pre-emptive basis. The Directive has been implemented by all the EU Member States.

Seventh Council Directive (83/349 of 13 June 1983[22]) defines conditions for the preparation of consolidated accounts by companies having subsidiaries (groups of companies). These conditions differ from those laid down by the Fourth Directive.

Consolidated accounts should be drawn by the parent undertaking if it:

- has a majority of the shareholders' rights in a subsidiary undertaking;
- has the right to appoint or remove a majority of the members of the administrative, management or supervisory body of a subsidiary body;
- has the right to exercise a dominant influence over a subsidiary undertaking under a contract or a provision in its memorandum or articles of association.

Consolidated accounts eliminated duplication of the assets and liabilities related to commercial transactions within the group of companies. By the end of the 1990s the Directive was implemented by France, the UK, Germany, Greece, Luxembourg, and the Netherlands.

Eighth Council Directive (84/253 of 10 April 1984[23]) sets rules on approval of physical persons and legal entities responsible for carrying out statutory audits of the annual accounts of companies. Under the Directive, each Member State has to ensure that the auditors are independent and fit to carry out statutory audits. Besides, the Directive defines educational and training requirements to be met by the auditors.

[19] OJ 1978 L 222/11.
[20] Directive 90/605/EEC (OJ 1990 L 317/60), Directive 90/604/EEC (OJ 1990 L 317/57) etc. Directive 90/605/EEC is designed to prevent a situation where partnerships are set up in order to avoid implementation of the above directives. Under the Directive public limited-liability companies are requested to provide name, head office and legal status of any enterprise of which the said public limited liability company is a full member. Besides, the document envisages obligatory keeping of accounts of every partnership member that should be subject to auditing and publishing its results. Directive SI/1992/2452 aims to ease the burden born by small and medium-sized companies because of the excessively stringent accounting rules. After the changes and amendments have been introduced, Article 53 (2) of Fourth Directive reads: "The Member States may permit companies which on their balance sheet dates do not exceed the limits of two of the three following criteria: balance sheet total – ECU 250 000 (ECU 200 000 before); net turnover: ECU 5 mln (ECU 4 mln before); average number of employees during the financial year: 50, - to draw up abridged balance sheets …»
[21] OJ 1982 L 378/47.
[22] OJ 1983 L 193/1.
[23] OJ 1984 L126/20.

Eleventh Council Directive (89/666/ EEC of 21 December 1989[24]) sets disclosure requirements separately in respect of branches opened by companies in a member State and in a non-member country. The Directive concedes that a branch can not be by itself recognized as legal entity and thus requires:

- that information (including the accounting entries) should be disclosed about the company of which the branch is a part, in accordance with the provisions of Directives Fourth and Seventh;
- that the accounts of the company must give a true and fair review of the position of the company or the group of companies.

Twelfth Council Directive (89/667/EEC of 21 December 1989[25]) was intended to introduce in the EU Member States legislation permitting single-member private limited-liability companies. Such companies should be allowed to exist in every EU Member State. The Commission believes that the permission to form a company with only one member (a physical person or a legal entity, i.e. a firm) stimulates physical persons to form new undertakings. One more advantage is that such a company acquires legal personality and can continue its activities even in case the owner is changed.

All the shares of such a company should be issued in the name of their owner who is the only shareholder. The sole member should exercise the power of the general meeting of the company; record in minutes the decisions taken by the sole member, and draw up in writing contracts between the sole member and his company. Otherwise the company becomes subject to the normal restrictions envisaged by company law.

Article 7 of the Directive provides an alternative: the EU Member States are allowed to introduce legislation providing that an individual entrepreneur may set up the undertaking the liability of which is "limited to a sum devoted to a stated activity", which is similar to private companies limited by guarantee. Each Member State of the EU has the right to introduce restrictions on activities of a person as the sole member of several undertakings and to make a decision on applicability of the Directive to public companies.

There is also a range of **draft Directives** in various stages of progress.

Proposals on **Fifth Directive** (internal structure of a company's management bodies, their structure and responsibility) were submitted to the CEC as far back as in 1972 but met a serious opposition (Le Gall, p. 81). The amended draft was sent to the Council on 19 August 1983.

Initially, the Directive was designed to introduce changes into company structures so that they had a two-tier management system (i.e. two Boards: the Executive Board and the Supervisory Board). At the moment the draft permits of adopting a one-tier management system (i.e. envisages one Board comprising members having executive and members having supervisory functions). Estimates show that the project in its present form is going to cause some technical difficulties in its implementation and overall is capable of just maintaining the status quo (giving shareholders the right to chose among the management structures).

In 1990 the EU Commission submitted to the Council a number of proposals on amendments to Second Directive on company law and to the drafts of Fifth and Thirteenth Directives on company law. One of the expected results should be widening of the scope of the "corporate democracy" in the EU Member States through:

[24] OJ 1989 L124/8.
[25] OJ 1989 L395/40.

- lifting restrictions and giving the shareholders equal voting rights (amendments to the draft Fifth Directive);
- imposing limits on the "golden share" practice that provides protection for some of the companies and results in open market asymmetry;
- regulating the situation where company's shares are being acquired not by the company itself but by its subsidiary (to minimize manipulations after take-over announcements through limiting the powers of the managing body of the company that received the offer) and giving the shareholders wider rights to nominate, appoint, and remove directors from office.

The provisions concerning employees' involvement were also subject to debates. The initial proposal to ensure such involvement through appointments to the Board was the only model envisaged by the Directive. Later on the idea was modified: employee's involvement became possible through "informed consultations" or through provision, under certain circumstances, of the right of veto over the decisions by the appointed Board members. However, even this wording met a serious opposition. Great Britain, for example, insisted that such provisions are not consistent with the corporate law. This position was not shared by the Netherlands and Germany as no clear-cut distinction between corporate and labour laws exists in these countries.

Apart from those fundamental issues the Directive was criticized for being excessively detailed, for the rigidity and complexity of the procedures of information and consultation of employees. The organizations representing business communities of Europe and individual countries (in particular, UNICE, CBI) and the Law Society expressed their concern that adoption of the Directive would increase the burden the companies carry in respect of regulatory procedures which would not be accompanied by a proportional increase in advantages for the company and its employees.

In the late 90-s the Commission continued the consultations covering, inter alia, a possibility of using the Directive on "European Works Council". In its Resolution of 17 January 1997, the European Parliament opposed the approach on the grounds that setting up such a body is not an equivalent of participating in the Board of Directors. The European Parliament proposes the following minimum standards: provision to company employees a seat on the "two-tier" Board of Directors or, in case of a single-tier Board, an opportunity to participate in making decisions concerning employees' economic problems and employer obligations should be a subject of an agreement with the company management.

In their final wording the Directives envisage application of practically every form of employee involvement that exists in the EU Member States:

- participation in the supervisory board with employees electing 1/3-1/2 of the member (the German model);
- participation in the supervisory board or in the executive body as an independent director through the system of co-optation (the Dutch model);
- establishing within the company of a special representative body – a consultative council comprising employees' representatives (the Danish model);
- system of collective agreements comprising elements of the above models.

Thus, the draft just notes the existing multitude of approaches (both to management structure and to employee involvement) which means lack of any unification. However, it is evident that a certain unification of public limited-liability companies' structure and functions of their management organs first of all to ensure equal degree of protection of the rights of the shareholders and other persons involved in the companies activities.

Draft proposals for **Ninth Directive** (not adopted by the Commission formally) were distributed in 1984. The proposals concerned behaviour of groups of companies. At present, according to some estimates, the draft has poor chances of being approved in the short term perspective.

It is appropriate to mention here the Directive on information and consultation of employees of groups of enterprises adopted by the Council [26] which stipulates that if the economic activities are to be developed consistently, companies or company groups operating in more than one EU Member State should inform and consult employees' representatives affected by their decisions.

Historically, this Directive is close to the so-called "Vredling Directive" that sets procedures of informing and consulting employees of companies having a "complex structure".[27] The Directive set requirements on informing and consulting employees of all the enterprises or groups of enterprises operating in more than one EC country and employing over 1000 workers out of which at least 100 work at two different enterprises in different EC countries. Such enterprises should establish a Council on European Employment problems that should become the venue for information and consultation of employees.

Draft Tenth Directive (mergers of enterprises of different nationalities, i.e. transnational mergers of public limited-liability companies) was submitted to the Council on January 14, 1985.[28] Tenth Council Directive deals exclusively with cross-border mergers for fears that such mergers might help bypass the provisions concerning employees' involvement. Thus, a consensus on the document and the issues it covers is yet to be achieved.

The Council adopted a number of Directives setting uniform requirements towards opening an access to the stock exchanges for securities (79/279 of 5 March 1979, 80/390 of 17 March 1980, 82/121 of 15 February 1982 and some others.).

Directive of 5 March 1979 coordinates terms of admission of securities to stock exchange listing.[29] Securities should not be admitted to stock exchange listing unless they meet the Directive requirements to legal status and minimum size of the company, free circulation of shares and the percentage of shares for public offering (normally, 25% and more).

Directive of March 15 1980 defines in detail the terms of admission of shares to stock exchange listing.[30] The information should be published by the official body in the form of "technical elements of the listing" before securities could be admitted to stock exchange tender. When the procedure is over in one of the EU Member State all the rest should recognize the terms of listing as sufficient. However, each of the Member States has the right to ask for additional information related to the specific market falling under its jurisdiction. The Directive also determines that as far as issue prospectus meets the Member State needs it can be viewed as a technical element of the listing.

A number of newly adopted Directives deal with "further disclosure of in formation", coordination of requirements to the issue prospectus, mutual recognition of prospectus as a technical element of the listing (D.,23 April 1990, etc.)

Directive on insider dealing contains rules envisaging physical or legal person responsibility for misuse of information on company if such information is related to prices. [31] The Directive sets minimum standards in the area which means the EU Member States are allowed to go beyond its

[26] OJ 254/64.
[27] OJ Vol 26C 217/3.
[28] OJ 1985 C23 28/11.
[29] OJ 22 L66/21.
[30] OJ 23 l00/1, OJ L185/81.
[31] OJ 32 L334/30.

boundaries. The Directive requests all the EU Member States to ban insider dealings and cooperate in the relevant information exchange to administer justice.

The Directive on investment services adopted in July 1993 envisages that "investment companies" should receive permission from their own governments that would serve as passports and allow them to carry out investment activities in the other EU Member States (Articles 1, 4).[32] The service can be provided within the EU irrespective of the national boundaries. Otherwise, the investment company can get a permission to open branches in the other EU Member States without necessarily obtaining a new permission.

It should be stressed that the EU Court of Justice is increasingly alert to the cases of failure to implement the Directives fully and does not hesitate to substitute its own interpretation of the regulation for the relevant provision of the Member State national legislation if it believes the latter provides a wrong interpretation of the EU act.

2.3. "The European Company"

The issue of establishing a European company has been on the EU agenda since 1965, the first draft being produced as far back as in 1970. Initially, two approached emerged.

The approach advocated by France envisaged the development of a Statute of a European-type company – a national undertaking acting on the basis of a special unified legal act. The common company law of a Member State should be applicable to the company in accordance with the principle of subsidiarity. The approach by the EU Commission was to form a company that would operate fully under the Common Market law and be its subject. A group of experts headed by Pr. P. Sanders developed a draft Statute of such a company that was twice (30 July 1970 and 13 May 1975) submitted to the Council as a draft Regulation. The draft copied to a considerable extent the German company law, in particular concerning the issues of employees' participation in the supervisory board and regulation of activities of groups of companies. [33]

A temporary compromise was reached with adoption on 25 July 1985 of the Regulation № 2137/85 introducing "European Economic Interest Grouping" – (EEIG) as a less complex and more flexible legal and organizational form of cooperation and centralization of capital.[34] The EEIG was designed as a new instrument of establishing an undertaking by citizens of at least two EU Member States. Making profits for itself should not be the main purpose of a grouping and the employers can not hire more than 50 employees. At the proposal stage the Regulation envisaged that R&D would be the basic function of such a grouping. However, at the moment the grouping form is used to resolve a wide range of tasks (see Anderson, 1990, p.9). One of the advantages of EEIG is "taxation transparency", i.e. profits are taxed after they have been distributed among its members.

The purpose of a grouping is only to facilitate or develop the economic activities of its members. A grouping has no authorized capital and its members have unlimited joint and several liability for the

[32] OJ 19898 L/386/32.

[33] The time spent on completing the procedure depends on a number of factors. The higher the complexity and inconsistency of the measure the more time is needed to implement it. Besides, progress in this area might depend on how much an important European official, President of the European Commission, for example, tries to implement the measure while he/she still occupies the present position.

[34] OJ 28 L199/1. Some researchers believe this form is not a compromise but an alternative and define it as a supra-national "trans-European institution" produced through "interbreeding" of a small company, a partnership (unlimited joint and several liability of participants, lack of a legal status), a non-commercial partnership, a cooperative, an association of legal persons (limited legal capacity, i.e. ability to carry out only activities directly related to the participants' activities. Consequently, EEIG does not fall into the area of company law regulation but is of interest as the first experience of creating a supra-national legal institution at the micro-level.

grouping's debts. In accordance with the national law of Germany and Italy, for example, an EEIG can not be a legal entity.

The Regulation left unresolved a range of important issues, such as internal structure of the governing bodies, legal capacity, bankruptcy, implications of unlimited joint and several liability, etc. These gaps should be filled up with national rules which means, that in spite of the Regulation being a direct-action document serious differences remain between EEIGs formed across the EU Member States.

The French legal institution functioning since 1967 and bearing the same name served as a model for the "grouping" (see. Jamin, Lacour, 1993). "Economic interest groupings" existing under the commercial law of France make it possible even for competing enterprises to save considerable resources (through joint purchase of raw materials or R&D). However, they much less often make direct profits. According to some estimates the introduction of the provision on simple-type public companies (1992) into the French legislation should result into a considerable reduction in the number of the groupings.

In 1991 the EU Commission made public a proposal on developing the Regulation and the Directive that together are known as European Company Statute - ECS [35]. The adoption of the documents was supposed to open the way to establishing a business which is partially subject to the European law (in accordance with the Articles of association) as and partially – to the law of a Member State where it will have its registered office. Thus, new opportunities will be open for businesses although the proposal requires neither all the companies to become "European" nor national corporate laws to be amended. Therefore, a business is given a chance of becoming a "European company" from the outset.

Only in 2001 the documents: Council Regulation 2001/2157/EC of 8 October 2001 on the Statute for a European Company (SE) and Council Directive 2001/86/EC on amending the Statute for a European Company to take into account employee involvement were adopted.[36] The documents shall come into force simultaneously in three years from the date of their formal adoption.

Procedural problems (the necessity to have a Council Regulation to be adopted by all the EU Member States by consensus) were cited as the official explanation for almost a 30-year-long delay in adopting the documents. Reaching a compromise on employee involvement is named as an important component of finding a common approach. Member States with strong employee involvement traditions are concerned with a possibility of a European company to be used to by-pass the national rules on employee involvement. Conversely, Member States having no such traditions feared that a European company would be used to impose on them additional requirements concerning employee involvement.

The Statute for a European Company is officially interpreted as a new legal instrument based on the EU law and permitting the creation of a European public limited liability company ("Societas Europeae" – SE - in Latin). The Regulation is directly applicable in all the Member States while the Directive shall be implemented within the framework of national law.

SE can be created within the EU territory in the form of a European public limited liability company. Four ways of forming a European public limited liability company are envisaged:

- public limited-liability companies may form an SE by means of a merger provided that at least two of them are governed by the law of different Member States;

[35] OJ 1991 C176/1 and COM (91) 174.
[36] OJ 2001 L294/1 and OJ 2001 294/22

- public and private limited liability companies may promote the formation of a holding SE provided that each of at least two of them is governed by the law of a different Member State;
- companies and firms may form a subsidiary SE by subscribing for its shares provided that at least two of them are governed by the law of different Member States;
- a public limited-liability company may be transformed into an SE provided it has for at least two years had branch situated in another Member State.

An SE may be formed as a public or as a private medium-sized company. The subscribed capital of an SE should be not less than 120 000 euros. If an SE's shares are traded, the process should be under the regulation applicable to public companies created in accordance with the national legislation. The Statute prescribes no restrictions concerning the type of commercial activities of such a company and the number of its employees.

This legal institution offers the following advantages:

- companies created in more than one Member State can merge and operate on the basis of a single set of rules, single legal structure, unified management and financial reporting structure;
- the necessity to create a costly (in terms of finance, administrative and legal effort) network of subsidiaries operating within national legal systems [37];
- within the given institution an opportunity arises of an easy and simple restructuring of the business to use advantagesв of the single internal market.

It is important to note that the Statute permits of transferring the seat of a company from one EU Member State to another without going into liquidation. Nevertheless, SEs should be registered at the national level with the relevant information published in the official EU publication.

Board of Directors (Supervisory Board) might or might not be among the management bodies (Articles 38-60 of the Statute). However, the national legislation of the country of SE registration can not prescribe any definite system of management (one-tier or two-tier). Under Article 38, an SE should comprise (a) a general meeting of shareholders and (b) either a supervisory organ and a management organ (two-tier system) or an administrative organ (one-tier system) depending on the form adopted in the statutes.

Thus, the company structure issue that had been a stumbling block for discussing the Fifth Directive was resolved by reaching a compromise that in fact fixes the multitude of national models.

Similar conclusions might be made on the issue of employee involvement.

SEs should follow a certain system of employee involvement in making decisions. In case of failure to come to a mutually acceptable agreement through a negotiations process, standard principles should come into force (Annex to the Directive). The principles oblige the SE managers to provide regular reports that should serve as a basis for regular consultations and informing the body representing the interests of the company employees. In some cases (formation of SE by merger, as a holding or a mutual venture) 25 % or majority of employees have the right to participate in making the company's decisions before the SE is formed.

According to some estimates, until now the harmonization programme has failed to produce "common European outlook" for companies. The reason behind the situation lies in the fact that the

[37] A company operating in several EU Member States are not obliged to abide by the Se Statute. However, cost cutting can serve as an incentive.

Directive-driven harmonization is not capable of reaching such a result as the implementation would require its incorporation into the national legislation. Contrary-wise, the Statute of a European Company brought into force by the Regulation opens an opportunity of reaching harmonization in that all the countries have a chance of establishing a single company structure. However, as legislative systems of the EU Member States to a considerable degree themselves fill the "gaps" in the Statutes (as was the case with the EEIG), there is a risk of producing 15 different types of "European companies".

2.4. Mergers and takeovers

2.4.1. Terms and models: some by-country differences

The problem of harmonization of the EU Member States legislation in this area is also to a large extent related to differences in the national models of corporate governance (see Chapter 1, and Belenkaya, 2001) and in business practices.

In countries of the Anglo-Saxon model of corporate governance mergers and takeovers are a traditional tool of corporate control. The well-developed (perhaps even excessively developed if compared with the real sector of the economy) stock market, diffusion of the share capital, cultural traditions ("an enterprise is nothing but a block of shares for the owner") contribute to the situation. The 80s–90s witnessed an upsurge in the number of mergers and takeovers. In the period of 1995–2000 in the USA 26 000 companies merged with the deals amounting to US $5 trillion. At the same time deals of this type underwent a qualitative change. While previously mergers and takeovers had been performed in the interests of strategic development of business and upon an agreement by the parties involved, the 80s–90s brought in an new tendency. Globalization of stock markets and new standards of information transparency resulted in the emergence of a new market player – "raiders" having as their aim an aggressive buying of the undervalued companies in order to increase their market value in the short-term and sell them later.

Many researchers believe that the takeovers market is the only mechanism of protecting shareholders against management's arbitrariness. They point to the fact that the method is most effective when it is necessary to "overcome" the resistance on the part of a conservative Board of Directors not interested in rationalization (breaking down) a company, in particular, when company diversification is involved (Coffee, 1988). The literature on theory of the issue offers a thorough analysis of the relation between takeovers entailing "private" (special) interests for large shareholders and an increase in economic efficiency after control passes on to a new owner.

At the same time criticism is increasingly leveled at efficiency of the method for corporate management purpose. In particular, it is noted that the threat of a takeover pushes managers towards implementing short-term projects only for fear of a downturn in share prices. The conflict between short-term and long-term business objectives makes companies take care, first and foremost, of increasing prices of their shares and current (quarterly) profits ("the tyranny of quarterly financial reports"). "Stock exchange pressure" as a reaction to the event acquires higher importance than the event. The ENRON affair is to some extent the result of the situation. Other critics believe that takeovers serve exclusively the interests of shareholders and do not meet the needs of all the "stakeholders". Finally, there is (empirically proved) risk of destabilizing of activities of both the buyer company and the acquired company (see Grey, Hanson, 1994).

In Europe (the continental "Rhein" model) enterprise has been traditionally viewed as not only as an exclusive property of the shareholders but also as a social institution accountable to all the stakeholders. Concentrated structure of ownership "chains" the enterprise to the strategic owner interested in its long-term development. "Friendly takeovers" (that are in fact mergers) prevail

while "hostile takeovers are rejected in principle and condemned by the society and by the business community. That is why raiders' operations are much less widespread than in the USA.

However, while in the second half of the 90-s in the USA the number of hostile takeovers decreased (from 1995 to 1999 the volume of transactions dropped from US $50 to 10 bln.) Europe became the world leader by hostile takeovers (Leonov, 2000). The share of hostile takeovers increased both in the total number of all the merger and takeover transactions and in the number of cross-country hostile takeover in Europe. In 1999, out of the total volume of US $1487 bln of all the mergers and takeovers in Europe, the share of hostile takeovers amounted to US $393 bln (i.e. was 4 times higher than in the whole period of 1990-1998). Intensification of the process necessitated adequate measures at the EU level.

The Japanese model is characterized by voluntary unifications. Hostile takeovers are subject to tough institutional and social barriers. The institutional barriers consist in the company management providing itself with "permanent shareholders" – normally they are companies from the same holding group ("kairetsu") or friendly banks. At the same time, cross-holding of shares is widespread. "Permanent shareholders" owning 60–80% of the shares remove the threat of taking over of the company through buying the shares on the market. Under the circumstances companies can focus effort on strategic objectives.

Social barriers mean that cultural traditions of the Japanese business consider enterprise as a community of life employees having an informal hierarchy and its own system of promotions. That is why "takeover" of companies with employees is severely condemned. Normally, employees, trade unions, administration and main shareholders take a united position in relation to the proposed transaction. For Western companies resistance by employees is the main obstacle when they attempt to take over Japanese enterprises. Perhaps the fact of "being close", the orientation towards internal sources of growth helped the Japanese economy to attain the sustainable economic growth in the post-war period and to become one of the three leading industrialized nations. However the stagnation of the 90-s might mean that this model of corporate governance has exhausted its potential and needs to be modified to increase its efficiency.

The recent empirical studies to some extent have weakened the interest to theoretical analysis of the "atomistic" corporation. In Japan and in the continental Europe countries, even the largest companies (with shares traded not only on the national exchanges but internationally as well) ownership and control most often are characterized by a high degree of concentration. In many cases the owner who acquired control is directly involved in the process of management. Under the circumstances the regulatory mechanisms inherent to capital markets might work in specific situations where "hostile" takeovers of underperforming companies become almost impossible.

Moreover, it would be safe to say that modern methods of company formation bring about a system of economic incentives that prevent breaking down of established large blocks of shares which would inevitably result in a drop in the company's market value (see Shleifer, Vishny 1986).

Overall, legislation of developed economies (see Kulagin, 1997, pp. 131-138; Shelenkova, 1998) envisage such forms of re-organization of legal persons as merger (two or more companies merge into one new company – a new legal entity), a takeover (oone or several companies join an established legal person), divisions (a legal person breaks down into two or more new legal entities), and split-off ((transfer of part of the assets to a newly established entity without liquidation of the company-donor).

In France re-organization of mutual enterprises companies (the law "On commercial partnerships" of 1966) is allowed in the following forms: fusion (unification of at least two established partnerships through one of them taking over the other or through forming a new partnership), division (transferring of the assets of one partnership to established partnerships), and fusion-

division (the partnership transfers its assets into established partnerships or participates in setting up new partnerships). The partnership acquiring as a result of the above operations all or part of the assets of the other partnerships becomes its legal successor.

The German legislation permits of mutual enterprises mergers in two forms: through transfer of the company's assets to another company in exchange for the shares and through forming a new mutual company that acquires the assets of the merged companies.

Both the legislation and the doctrine lack a concerted opinion on what should constitute a takeover bid. The following specific features of the institution are usually identified:

- this is a public offer to buy the shares of a certain company under terms stipulated by the tender offer;
- the bid should be addressed to all holders of securities of certain classes;
- the bid should be made by a corporation.

Making a mandatory bid might be subject to a number of conditions: acquisition of the company can be made subject to an agreement by the general meeting (see p. 2, Article. 80 of the RF law "On Corporations); shareholders might be given the right to put forward conditions for acceptance of the offer; a partial offer covering 2/3 of the total number of ordinary shares can be made.

Nevertheless, in England this institution to a larger degree is associated with the concept of "takeover bid" as in accordance with the English law the aim of the operation should be to acquire control over company that has its shares being bought. In France Bthose who initiate such an operation might try to use it not only to acquire but also to solidify control over a company (in Russia solidifying/widening of control served as the main incentive for takeovers before 1998). In any case an operation aimed to acquire less than 15% of the company's capital cannot be considered as a takeover bid.

In Great Britain, the City Code on Takeovers and Mergers envisages that acquisition price can not be below the highest price at which the offeror acquired such shares within the last 12 months. In accordance with the German Takeovers Code acquisition price should not drop below 25% of the price at which the offeror acquired the company shares within the 6 months prior to reaching the percentage threshold (under the Russian legislation — not below the average weighted price of buying shares within the 6 months prior to the date of acquisition of at least 30% of the shares). There are differences in timing of mandatory bids: in Great Britain it should be made immediately, in Germany – within 21 months from the moment of reaching the percentage threshold.

The issue of what should be the threshold for making a mandatory bid is also a controversial one: in Great Britain — 30%, in France — 1/3, in Germany — 50%, in Denmak, Belgium, and in Italy — acquisition of control over the company.

For the purposes of the present study it would be reasonable to apply universally accepted definitions used in the theory of corporate finance and the world practices of such operations. [38] The following three forms of corporate control are widely used across the world and account for over 85 % of the total volume of transactions (see Roudyk, Semenkova, 2000; Roudyk, 2001).

1) Merger – is normally a synonym of a friendly takeover (in other interpretation – a financial transaction resulting in a merger of two or more corporations into one accompanied by converting of the shares of the merging corporations, maintaining the owners and their rights).

[38] See Radygin, Entov (2002a)

A merger is an agreement between management groups of the buying company and the target company concerning the selling of the latter. Managers of the company being acquired should enter into negotiations concerning the merger only after the negotiations have been approved by its Board of Directors and shareholders. Thus, a merger is first of all a contract between the management groups of the two companies worked out in the course of negotiations. During such negotiations managers of the corporation being acquired first of all play the role of agents of the shareholders.

2) Takeover - is a paid-up transaction resulting in transfer of corporate ownership rights and most often accompanied by changes in management of the acquired company and in its financial and production policies. The deal involves two parties – the buying company and the target company.

The following variants of takeovers are possible: a) the buying corporation makes a tender offer (an offer to buy-out 95-100 % of shares of the target company) to the target company management (friendly takeover); b) the buying corporation makes a tender offer to the target company shareholders to buy-out a controlling block of ordinary voting shares by-passing the management (hostile takeover).

Tender offer should be made public and executed irrespective of its approval/non-approval by the target corporation management. In this way a hostile takeover results in removal from office of the target company management. In theory, acquiring a controlling interest (50%+1 ordinary voting share of the target company) is enough to successfully finalize a hostile takeover of any corporation.

As a "business-term" hostile takeover implies an attempt to acquire control over economic activities or assets of the target company against the wish of its management or the main participants. Referring the transaction to the category of "hostile ones" depends largely on the target company management and/or shareholders/participants reaction (the usual practice in Russia) if the attacking company has met all the requirements by the regulatory authorities concerning the publication formalities (Leonov, 2000).

3) LBO–leveraged buyout is a financial tool (not an operation) applied from the mid-80s to transform a public corporation into a private one. A group of external or internal (managers) investors buys out all the corporation shares that are in circulation with 80-90 % of the resources needed to buy them out raised through emission of debentures (most often trash/high-yielding securities). In 3 to 6 years the shares return to the open market, although cases are known when companies remained private.[39]

Apparently, re-organization of legal persons is prone with many problems related not only to control by the government bodies over concentration of economic power and widening of legal capacity of companies taking over other enterprises operating in the other sectors of the economy (see Kulagin, 1997). Of no less importance are the problems of protection of the interests of shareholders who disagree with the re-organization plans and company creditors participating in the operation that should be resolved within the national (or a uniform, European, for example) legislation.

In this connection mention should be made of the mixed feelings researchers have on takeover bid. Some authors believe it is an institution designed to protect the interests of minority shareholders (better terms of selling shares than at the stock exchange plus indirect control by the management) while others are less optimistic. An offer to buy-out shares the controlling group makes to minority shareholders might be preceded by certain moves (lowering the dividends, manipulating the

[39] Acquiring control over the Board of Directors without buying the controlling interest in the share capital through proxy vote can be viewed as the 4th form.

information) aimed to lower the market prices and to produce an illusion that the deal is beneficial for the minority shareholders. Hostile takeovers might present similar problems.

2.4.2. Regulation of mergers and takeover in the EU law

The issue of powers to control **mergers** by the EU institutions was raised practically immediately after the Treaty of Rome came into force.[40] The problem was related to the fact that Articles 85-86 concerning competition and abuse of dominating position on the market did not provide for direct control over mergers. In 1972 and 1987 the European Court set precedents by ruling that Articles 85-86 were applicable to mergers under certain circumstances (for example, buying a large block of shares under condition of additional purchase of shares in future that would result in changes in control over the company). In 1989 the Council adopted Regulation 4064/89 (the unofficial name – "Regulation on Mergers") which set criteria for referring mergers to the EU Commission competence and procedures of making the necessary decisions.

To the Regulation (and to refer the case to the exclusive competence of the EU Commission) the total world turnover of all the companies involved should exceed 500 bln euros and the total turnover within the EU territory should reach 250 bln euros. The companies should notify the EU Commission within one week after buying the controlling interest, publicizing the information about the tender or signing an agreement.

Importantly, the Regulation uses the term "concentration" which is essentially an economic term covering a wide range of transactions resulting in concentration of control. Regulation defines the following methods of concentration:

- merging two previously independent companies;
- acquiring direct or indirect control over company (companies) through buying out shares or assets with signing a contract or without signing a contract;
- the so-called concentrated mutual enterprises (agreements aimed to acquire control over actually a single economic entity).

In practical terms the following schemes are most often applied: acquiring personal control, acquiring joint control, acquiring joint control over a mutual enterprise, and switch from joint to personal control. It is believed that the regulation happened to be a very efficient tool of carrying out competition policy within the EU. After its adoption the EU Commission started to receive 50-60 notifications a year – the figure that has doubled by now.

The problem of regulating **takeovers**[41] has been under discussion within the EU for over quarter of with a varying degree of intensity (the 1974 Pennington Project, the direct recommendation in the 1985 EU Commission White Book on adopting a special Directive, etc.). Originally, the proposal on the project under discussion (the so-called Thirteenth Directive "Directive on Takeover Bids" was adopted by the EU Commission in 1988. In February 1996 the Commission issued a new proposal characterized as a "framework directive". Draft Directives were repeatedly reviewed by the EU in 1989-2001.[42]

[40] See Entov 2001; Brittan, 1991; Cook, Kerse, 1996, and Anners, 1996; Puchinsky, Bezbah, Ermakova et al., 1999; Borko, Kargalova, Yumashev, 1995; Nickerov, 1999.

[41] Hereinafter the term "takeover" is used in the meaning it has in England, i.e. by its economic content it is most close to defining a transaction aimed to acquire a stock company. As mentioned above in England the term «takeover-bid» corresponds to the notion "an offer to acquire control". These terms – "takeover" and "takeover bids" are used in the English copies of EU documents.

[42] OJ 32 C64/8 and COM (95) 655 final. Unlike in case with mergers where a possibility of supra-national regulation is based on the EU Court rulings, the EU Commission does not have an exclusive competence in the area of takeovers

The general approach to regulating takeovers at the EU level has certain peculiar features:

- use of the principle of subsidiarity [43]; the EU acts in accordance with the "comparative efficiency" criterion", i.e where national regulation is deemed insufficient and the potential operations in terms of their volume and result could be better performed at the EU level;
- lack of a "single playing field" (as a consequence of retaining national legal barriers) in the area set additional objectives for regulation (apart from the traditional ones, such as protection of investors and proper functioning of capital markets): establishing a new order of business activities as a prerequisite for free market competition;
- most of the provisions of the Directive set only general (framework) principles of regulation and minimum harmonization standards while developing details remains in the competence of national law-maker (EU Member States can retain or introduce tougher national takeover regulation).

The following provisions of the draft merit to be mentioned specifically[44]:

- equality of the offeror and the offeree companies (Article 5 (1) of the draft),which means, in the most widely accepted interpretation of national laws, that all holders of shares of the same class should be treated equally;
- prohibition of manipulations on the securities market (taking into account insider activities): a bid should not result in structural changes in trading inn securities of the offeror and the offeree (Article 5 (1) d of the draft);
- transparency of the bid (Article 6 of the draft): shareholders of the offeree company should have the documents necessary to reach a properly informed decision.
- two requirements were set for the offeree company: neutrality of the management body and the obligation to of the board to draw up and make public its opinion on the bid;
- protection of minority shareholders.

The last issues is in fact the fundamental one and represents a compromise between the British and the continental law approaches.

First of all, it is related to the obligation to bid for acquiring shares of the "minority". This requirement is characteristic of the countries of common law. It was fixed for the first time by the 1972 English City Code on Takeovers and Mergers. In 1974, a limit of 30% of voting shares was set for the offeror and its affiliated persons. By now most of the EU Member States (Germany, Austria, France, Belgium, Denmark, Italy, Spain, Ireland) introduced this norm in their anti-monopoly legislation and codes (for example, the 1995 Takeovers Code in Germany) or stock exchange regulations (see also p. 2, Article 80 of the RF law "On Corporations". Nevertheless, in a number of countries (Sweden, to some extent Belgium and Germany) doubts have been raised concerning effectiveness of a mandatory bid.

In view of the above (the draft Directive) the EU Member Countries should prove availability of regulations, rules or procedures that oblige persons who acquired a certain percentage of shares to make a bid (an offer) or set some other equivalent means of protecting minority shareholders

regulation. Therefore, as far as takeovers are concerned the Directive (not the Regulation) can be applied as a European legal act.

[43] For the first time this principle was fixed by the new wording of Article 130 of the EU Treaty adopted in the Single European Act. At present, Article 3 b II of the EU Treaty is under discussion.

[44] The draft Directive does not prescribe any procedure of acquiring a company (making a bid, its change and withdrawal, access for competing bids, etc.) as this is within the competence of national law-maker.

(Article 3 of the draft). As a result the obligation to make a bid to acquire shares of the minority shareholders is devoid of its absolute character within the project. The choice should be made within national legal traditions.

In accordance with Article 10 of the draft Directive the offeror should make an offer to the shareholders to buy out their shares "at an equitable price". Consequently, the problem of acquisition price should be resolved by national legislations.

A compromise (draft Directive, 1996) variant is envisaged also for the percentage threshold which defines the necessity to make a bid. This issue is referred to the competence of the national law of the country where the offeree has its seat (Article 3).

One more problem is related to by-country differences in merger regulation. Germany and the Netherlands are known to have a stringent state supervision over company acquisitions, well-developed cartel legislation and procedures of negotiations with the company employees. The regulatory system of Great Britain and Ireland is based on the principle of self-regulation and extra-legal execution of takeovers (for example Great Britain applies the non-statutory City Code on Takeovers and Mergers non-judicial Panel on Takeovers and Mergers. The principle of voluntary compliance helps to reduce the number of legal disputes in courts[45]. Mixed regulation is characteristic of France, Belgium, and Spain.

It is important that in Great Britain "self-regulations" has a meaning different from its meaning in the counties of continental law. In these countries self-regulation and self-control have lost their initially autonomous nature and have been embodied in legislative provisions. Codification of provisions concerning insider activities within the EU is the most vivid example. A similar position in relation to takeover regulation was taken by Switzerland, where a voluntary takeovers code of 1989 was transformed into provisions of the law "On stock-exchanges and stock trading" of 1995.

The draft Directive envisages availability of national control bodies and the necessity to coordinate their activities (Article 4). However, these functions could be performed by private organizations as well. At the same time it is determined that the voluntary self-control method should be used to avoid involvement of administrative and judicial bodies in resolving takeover issues.

The above provisions of the draft demonstrate that its predominantly general character in fact preserves national features of takeover regulation in the EU countries. As in the case of the "European company" the conflict of national approaches results in lengthy discussions and the search for compromises that leave supranational regulation drained of its content.

The problem of resistance to innovations in the area should also be taken into account. In 1993, 5 out of 12 EU Member States opposed adopting the EU Commission Directive on regulation of merger and takeover transactions. An analysis shows that these countries account for 70 % of such operations and for 94 % of all attempts of hostile takeovers (Kobyakov 1997). Germany – traditionally viewed as a country of "adequate" corporate culture - occupies a prominent position among those countries.

The latest draft Thirteenth Directive on Takeovers was rejected on 4 July 2001 by the EU Parliament vote. Frits Bolkestein, Member of the EU Commission, said the decision was disappointing.

In this connection, establishing in 2001 of the High Level Group of Company Law Experts means that the Commission is committed to move forward and to introduce in 2002 a new proposal taking

[45] The draft Directive contains a number of rules that could be found in the City Code on Takeovers and Mergers. However, many British analysts believe this will result in more litigation and lower flexibility of the body that will control regulations than is the case with the existing Takeovers Committee.

into consideration a widest possible range of opinion. In late 2001, taking into account the position taken by the EU Ministerial Council and the European Parliament during the discussions about the draft Directive (MEMO/01/255) the Group presented a report focused on the following issues:

- how to ensure a level playing field in the EU concerning the equal treatment of shareholders across Member States;
- the definition of the notion of an "equitable price" to be paid to minority shareholders;
- the right for a majority shareholder to buy out minority shareholders (the "squeeze-out procedure").

The following key proposals by the Group that will be reviewed by the EU at a later stage merit a special attention:

- "a level playing field for takeover bids": where the offeror acquires 75% or more of the share capital of the company being bought as a result of the bid[46] he should be able to control the Board of Directors and the constitution of the company being bought in proportion to his share in its capital irrespective of any provisions in its constitution or articles of association against such control;
- "equitable price": if the offeror takes control over a company the price to be paid for the remaining shares in accordance with the Directive should normally be equal to the highest price paid by the offerror for shares of the relevant class during a period of 6 to 12 months preceding the date of the acquisition including the period of acquiring the control;
- "squeeze-out procedure": if the offeror acquires shares of the company in excess of the set percentages (between 90 to 95%) or, alternatively when his bid is accepted by owners of 90% and more of the shares, the offeror should have the right to buy out the minority shares at an equitable price (an "equitable price" is the price of the initial offer). Conversely, when the offeror acquires shares in excess of the set percentage (similarly, between 90 to 95% of all the shares) a minority shareholder should have the right to compel the majority shareholder to purchase his shares from him at an equitable price.

The Group believes that shareholders across the EU should have similar opportunities and rights concerning the takeover procedure, i.e a "level playing field". Therefore, any European company law should be guided by two principles:

- in the event of a takeover bid the ultimate decision must be with shareholders (not with the Board of Directors): they should be able to decide whether to tender their shares to the bidder and at what price;
- there should be proportionality between risk-bearing capital and control: only share capital which has an unlimited right to participate in the profits of the company or in the decision on liquidation, and only such capital should normally carry control rights, in proportion to the risk capital.

In view of the above the Group made the following recommendations:

- listed companies should be required to disclose complete information about their capital and control structures (with continuous updating of such information);

[46] The term «risk-bearing share capital», is used in the English-language copy of the Group Report. Essentially it means "securities the owners of which take part in company profit sharing".

- after actual announcement of the bid, the Board of Directors of the offeree company should be permitted to take actions frustrating the bid only upon authorization by the general meeting of shareholders (by a majority vote)
- after acquiring a certain percentage of the share capital (the threshold should not be set at higher than 75 % across the EU) the bidder should have the right to repeal immediately all the protective mechanisms (in constitution and in the control structure) that hinder the exercise of his control rights;
- the "break-through" rule should be applicable to the "golden share" giving special control rights to the EU Member States (within the powers provided by the EU legislation the countries wanting to retain control over companies should achieve this through adopting a relevant legislative act based on the common law principles);
- the restrictions on the transferability of shares (envisaged by the company constitution) should not be enforceable on the bidder;
- the EU Commission should rule when pyramid structures, circular or cross-shareholdings between companies should be regulated and what adequate measures of protection of minority shareholders should be enforced in all the EU Member States.

2.5. Bankruptcies

The EU Convention on Bankruptcy is one of the main documents in the field. It aims to provide a uniform framework for insolvency in a situation when company assets are spread across more than one EU Member State. The idea is to establish a procedure for "primary" liquidation or bankruptcy carries out by a "liquidator" having the right to operate in other countries where the company has its assets. If there is a need to carry out a "secondary" bankruptcy on the territory of another Member State, such a procedure can be initiated only as a subordinate one (in relation to the "primary" one).

The EU Convention on Bankruptcy was adopted in October 1995 and signed by all the EU Member States except for Britain. In accordance with Article of the Treaty the Convention is applied to cases of insolvency that involve disinvestment of the debtor. It excludes such procedures of saving companies as, for example, appointment of external administration (Great Britain). The proposal and the Convention cover insolvency of both companies and private persons.

As far as opening of insolvency procedures is concerned, the governments of the countries that are centres of the debtor's vital interests have jurisdiction over them. The approach is based on the assumption that for a company or any other legal person the centre will be in the country where it has its registered (or established by the constitution) office. In such cases the insolvency legislation of the country where the proceedings were initiated should apply. Nevertheless, the Convention permits of initiating insolvency proceedings under two and more jurisdictions – i.e. under different laws applied to one bankruptcy case. Consequently the law of universalism (i.e. one law covering the entire case) is not applied in such cases, which inevitably brings about legal conflicts.

The Convention defines that an insolvency case initiated in accordance with the law should be recognized by all the countries – signatories and have there the same legal.

Directive 80/987/EEC of 20 October 1980 (Francovich Directive) deals with protection of employees in cases of the employer insolvency.[47] Failure to observe the Directive resulted in the European Court ruling on legal cases C-6 and 9/90, Francovich and Boniface v. Italian Republic [1992] ECR 113). A certain Italian company initiated a process its liquidation in view of insolvency

[47] OJ L 1980 283/23.

and left the suer without wages he was due. Italy lacked compensation schemes for such situations and the became the grounds for the writ to the government to satisfy the requirement.

Chapter 3. Russia's corporate legislation and perspectives of applying the EU experience

3.1. Reception and general tendencies in development of company legislation in the period of transition

The second half of the 80 – 90s of the XXth century is characterized by a wide-scale borrowing of legal rules, of the EU first of all, by transition economies. Of course, transitional economies are a separate case, as here the issue is not convergence but an objective borrowing of the above models (their elements) or rebuilding of the historically developed legal system of the country. So far, the German model has been most widely accepted (at the law level) by the transitional economies in Europe (see also Radygin, Entov, 1999).

Nevertheless, the situation has been complicated by many new objective and subjective problems.

In the most general terms the basic institutional problem lies in the specific nature of a transitional economy as "non-cyclical systemic swing" in the economic development (Kuznetsov, 1994, pp.5-6). The institution of corporate governance, being such a principally new institution, not only bears the burden of the "systemic swing" but also directly depends on the situation with the other emerging institutions, tendencies in the reform and society development.

Among the most important specific problems characteristic (in this particular context) of most of the transitional economies and creating additional difficulties to forming models of corporate governance and control the following ones merit special attention:

- relatively unstable macroeconomic and political situation; [48]
- weak financial situation of a considerable number of newly established corporations;
- underdeveloped and overall contradictory legislation;
- extreme weakness of the infrastructure needed to enforce corporate legislation;
- dominance of large corporations and the problem of monopolism;
- in many cases a considerable initial "diffusion" of share ownership;
- special role played by managers (directors) in corporate control;
- on-going struggle for control over corporations and, consequently, instability of the ownership rights system;
- social and political barriers to carrying out real bankruptcy procedures of loss-making corporations;
- weak and non-liquid (low-liquid) markets of corporate securities;

[48] For obvious reasons the paper can not provide a review, even a short one, of the general macroeconomic and political problems affecting, in one way or another, the situation in the area of corporate governance (see: Glinkina., 2002). Besides, as mentioned above, corporate governance model is sufficiently resistant to radical modifications and any such influence can be normally indirect only (it becomes stronger under conditions of unstable economic and political situation of the transitional period).

- underdeveloped system of financial institutions;
- problem of transparency of issuers and markets related to the wide range of other problems (effectiveness of the tax system, etc.);
- consequent lack (weakness) of external control over managers of the former state-owned companies;
- weak internal (national) and fearing additional risk external (foreign) investors;
- lack (loss) of traditions of corporate ethics and culture;
- retaining a considerable share of property by the state;
- corruption and other criminal aspects.

Naturally, none of the transitional economies has corporate governance legislation (in the wide meaning of the term and taking into account all the interrelated legal acts) that could be viewed as a well-developed one. The legislation that does exist "…reflects what should exist or, in the best of the circumstances, what is emerging rather than what is already in place...It is something resembling the first stage of law development..., but it benefits from the fact that it can draw on the international experience and thus avoid the period trial and error...In this case, priority of the continental law is undisputable which, however, does not exclude a possibility of using certain good solutions offered by the English-American law... (Corporation..., 1995, Ch.VIII-IX).

Table 2. "Standard" elements of corporate legislation and their presence in some transition economies, 90s. *

	Russia	Czech Republic	Hungary	Bulgaria	Poland	Romania
Legislative acts акты	Civil code (1994), law "On Corporation" (1995)	Commercial code (1991)	Law VI "On business societies" (1988)	Commercial law (1991, 1994)	Commercial code (1934 with amendments)	Act "On business societies (1990) based on the Commercial code of 1887
(1) Clear-cut responsibilities for decision-making	Weak	Present	Present	Weak	Present	Weak
(2) Management structure (one or two-tier, i.e. board of directors and supervisory board	Two-tier if the number of shareholders is over 50	Two-tier always	Two-tier always	Depends on decision by shareholders	Two-tier if share capital exceeds 0.5 mln zloty	Depends on decision by shareholders
(3) Appointment of directors (votes required);	Over 50 %	Over 50 %	Over 50 %	Over 50 %	Not fixed, some can be appointed by large shareholders	Board's competence
(4) Removal of directors	Over 50 %	Over 50 %	Over 50 %	Over 50 %	Over 50 %	Over 50 %
(5) Control over voting right (by	Present	Present	Present	Present	Present	Present

proxy)**						
(6) Information discloser rules and audit;	High level	Low level	High level	Low level	High level (close to that of EU)	Low level
(7) Rights of minority shareholders:						
(a) preemption right of buying shares;	Present	Present	Present	Present	Present	n/d
(b) qualified (higher) majority for making important decisions;	75 %	66 %	75 %	2/3 of the authorized cpital	Can be 50% , 2/3, 3/4, 4/5	2/3 от 75 % of the quorum
(c) takeover rules;	Present	None	Present	None	n/d	n/d
(d) cumulative voting;	Present	n/d	n/d	n/d	Present	n/d
(e) limited number of voted per shareholder	n/f	Can be	Can be	n/f	Can be	Can be
(8) Employees participation in supervisory board	n/f	1/3-1/2, if number of employees exceeds 50	1/3, if number of employees exceeds 200	n/f	n/f	n/f
(9) Minimum for the general meeting quorum	Over 50 %	30 %	Over 50 %	по уставу	n/f	50 %
(10) Number of votes per share	Normally, 1	1	Not limited	1	From 1 to 5	1
(11) Ban on insider deals	Present	Present	Present	Present	Present	Present
(12) - Enforcement of the above norms	weak	weak	weak	weak	weak	Weak

** n.d. – no data available, n/f – no provision found in the legislation. The information might be outdated.*
*** actually depends (a) on rules of access to shareholder registers (b) prospects of establishing a system of depositories similar to the German one (where deposit banks vote for shareholders who express no opinion on the issues raised at the general meeting. The latter is in contrast with the US rules where such votes are nullified).*
Sources: RF legislation; Bohm A., ed., 1997; Grey, Hanson, 1994; Corporation, 1995; EBRD, 1998.

Although a certain standard set of corporate norms is present in majority of legal systems of transition economies (Table 2), the range of emerging models is very wide and covers most contradictory approaches:

- on the one hand, predominant orientation towards increasingly complex and detailed corporate legislation alongside the development of real processes and practices of corporate control (so far this happens in the countries that were the first to start privatization - Russia, Lithuania, Czech Republic, Poland, Hungary);
- on the other hand, the concept of the state moving completely away from the corporate governance problem. As an example, one can take Estonia where the main emphasis was made on a combination of "concentrated ownership" as the basic "panacea" and the policy of an indirect regulation by the state (competitive environment, taxes, introduction of international standards of financial reporting and accounting to provide a real access to the information and exercising control over activities of the board of directors). The approach is

evident in treatment of the government minority blocks of shares that private shareholders are allowed to "dilute" without fear of any consequences or sanctions.

In the mid -90s more "original" general interpretations of the concept of corporate governance and state regulation were known. For example, in Ukraine corporate governance and regulation policy in the area were interpreted in the following way:

- social protection of "citizens" and "employees" (sanctions against legal entities and managers violating "social liabilities" of the company);
- an increase in the role played by "employees" in the corporate governance;
- widening of the rights of the state as an owner.

In a similar way the problems of corporate governance were perceived in Slovakia. An increase in the role played by employees and retention of the state's role were considered as first priority tasks. In Uzbekistan, corporate governance was interpreted as principles of relations between PLCs and branch ministries. [49]

An attempt to analyze the formal ways of developing the relevant legislation (principles of codification of corporate law) shows that the countries under review can be classified as different groups. [50] Obviously, to a considerable extent this is a result of a traditional influence of the pioneer countries in Europe - France (Civil and Commercial Codes of napoleon of 1804-1807) and Germany (Bismark's Commercial Code of 1897).

The basic divide is normally provided by availability in the country of traditions of civil law (France, Germany and dependent countries) or common law (England, USA and dependent countries). Given the predominant influence of the Roman law, different authors identify from two to four by-country models: (1) Romano-German (continental, codified, source - law) and English-American (insular, "common law", without law branches, source – a judicial precedent); (2) French, German and English-American; (3) French, German, Scandinavian and English-American.

Continental Europe, like Russia uses universally adopted division of law into public law (organization of the state and its relationships with private persons) and private law (regulation and protection of interests of private persons). Private law, in its turn, is divided into two main parts: civil law (general rules regulating relationships between private persons) and commercial law (relationships between private persons receiving profit). "Commercial partnerships" ("business partnerships and companies") are viewed as falling within commercial law, while "corporations" in their turn are viewed as belonging to the category of "commercial partnerships" ("business partnerships and societies"). [51]

Some countries of Romano-German orientation are characterized also by the so-called "dualism" of private law – availability of both Civil and Commercial Codes (France, Germany, Spain, Greece, Turkey, Japan). "Monistic" private law (i.e. regulation of norms of commercial law within the framework of a single Civil Code) is characteristic of Switzerland, Italy, some other countries, and is adopted in Russia.

[49] The evaluation was performed on the basis of an analysis of the 1996 official reports by representatives of those countries to the CEEPN conferences. see.: Bohm, ed., 1996-1997.

[50] For more detail on classification see: Bogatykh, 1996, pp. 9-33; Basiliev, 1993; La Porta, Lopez-de-Silanes, Shleifer, Vishny, 1997.

[51] The trend to single out commercial law as a separate branch, in spite of the traditional system of "common law, was registered in the English-American system in the middle of the XX century. Those countries adopted , a number of acts aimed to simplify and modernize law and to repeal outdated precedents (Bogatova, 1996, pp.25-26). For example, in England one of such acts was the "Company Law" of 1985 and in the USA – a standard "Law on Business Corporations" adopted in many states of the USA.

Another, in fact, formal difference is availability (or non-availability) of detailed provisions of corporate law rules in special legislation. Special laws (apart from the Codes) concerning corporations have been adopted by most of the countries, for example, in France (Law on Commercial Partnerships of 1966), Germany (Law on Corporations), Switzerland (Law on Liabilities), Japan (Law of 1951), and others. Contrariwise, in Italy activities of corporations are regulated by the Civil Code.

One more difference is in the "weight" of a special law in relation to the code. The French law "On Commercial Partnerships" of 1966 in combination with the Decree "On Commercial Partnerships" of 1967 is in fact an independent new code providing a comprehensive regulation of corporations. In other countries such a special law may repeat or provide some more detail of the corporate norms that are already envisaged by the Civil (Commercial) Code.

Finally, codes might be further developed through adoption of a special law on corporations or a law providing additional regulation of activities of various types of business partnerships and societies.

Practically in every transition economy corporations are subject to some type of legal regulation.

Hungary was the first to follow the French way – to adopt a special detailed company law (Law on Business Societies of 1988 with Amendments of 1991). Naturally, the Law (300 Articles) was slightly less detailed than the similar French one. In addition to corporations it regulates also limited liability partnerships and other types of partnerships. Similar laws (that regulate corporations alongside other types of societies or partnerships) have been adopted in Albania, Bulgaria, Kazakhstan, Mongolia and Ukraine.

In 1991, Czechoslovakia (Czech Republic and Slovakia later) chose another way by adopting a Commercial Code covering a wide range of issues related to commercial law. Rights of partnership occupy an important place in the Code but do not dominate it as is the case in Hungary. The Code also regulates activities of cooperatives, contractual relations, some types of commercial obligations, competition, keeping of trade registers and accounting. Commercial codes have been adopted also in Poland, Macedonia and Estonia. The Bulgarian Trade Law can be in a certain sense also viewed as a commercial code.

According to some estimates, regulation of the rights of partnerships within the framework of commercial codes is not as detailed as in special laws. As is seen from the practice (including that in France and Germany) such regulation is characteristic of the initial stage of corporate law development. At a later stage provision of more details becomes necessary especially in view of the fact that in this area regulation by by-laws branch guidelines is extremely unadvisable (Corporation., 1995, c. XII).

By the end of 1996, special company laws were adopted (irrespective of availability of civil codes) had been adopted in Russia, Armenia, Lithuania, Moldova, and Tadjikistan. Overall, Roman-German traditions of law obviously dominate in the transition economies under the study.

However, there are certain objective differences at the level of fundamental trends in law evolution. When comparing corporate law (in the wider sense of the notion, as a set of rules on behaviour of organizations, companies) in Russia and economically developed countries some researches point to the general tendency related to the specific character of transition from centralized to market economy (Kashanina, 1995, pp. 367-369). In developed nations corporate law has a tendency to narrow down while the body of laws is increasing steadily. Contrariwise, in Russia a process of an intensive widening the area of corporate law is observed.

Apparently, the above formal differences in principles of codification and extension of corporate legislation do not testify about significant real progress in the area of corporate governance and protection of investors' rights in the countries reviewed.

Nevertheless, an evaluation performed with the use of formal criteria shows that to a certain degree progress has been made in the transition economies (see EBRD, 1997-2001 for more detail). Moreover, surveys by the Max Plank Institute of Comparative Law Studies (Hamburg) demonstrate that at the moment the CIS countries, unlike CEE and Baltic countries, have a stable tendency towards moving to the English-American model of protection of shareholders' rights. Forming the system of protection characteristic of the common law norms takes place in the CIS in spite of the traditions of civil law. At the same time in Central Europe adherence to the German model with its greater emphasis on protection of the creditors' rights persists (Pistor, 1999). It would be enough to look at the law "On Corporations" (and the Amendments of 2001) and to analyze the norms that make it possible for minority shareholders to officially defend their rights to get evidence this really happens.

Transition to new conditions of corporate development is accompanied by changes in the mechanisms of delegation of authority and direct and indirect monitoring. Development of the corporate governance system often generates processes that can not be considered optimal. One of such examples is, perhaps the wave of conglomerate mergers in the USA in the late 60s - early 70s private shareholders. However, active operation of forces of competition on various markets not only delineates (in the long term) possible limits of such deviations but most often triggers the mechanisms of de-centralization that correct the identified irregularities. Consequently, functioning of a developed system of competitive markets of goods, capital and labour markets remains to be the most important prerequisite to efficiency of corporate governance.

3.2. Specific features of potential harmonization of company law in Russia

3.2.1. Formal criteria

As was demonstrated in section 1.2 above none of the existing models of corporate control is perfect. In the same manner, none of the countries has reached the 100% level of implementing the 1999 OECD Principles of Corporate Governance 1999 (/OECD, 1999). The most developed countries, first of all those belonging to the English-American legal system (USA, Canada, Hong-Kong) have made the greatest progress along the way. They are followed by the countries of continental law, first of all by those that retain traditions of the Napoleon Codes (see IKPU, 2001).

For Russia most relevant would be a comparison with the so-called emerging markets. The first myth that should be demolished is that of the unique scale of violation of shareholders' rights in Russia.[52]

Originally, the interest towards corporate governance in Russia emerged only after the 1992-1994 mass privatization process was over, although the importance of the long-term nature problem for Russian companies had been understood by some economists and legal experts before. The law "On Corporations" (N 208-F3 of 26 December 1995) was an important legal benchmark. However, one can argue that the discussion about corporate governance (or rather about outsiders' discrimination) acquired a practical dimension as a result of the 1996-1997 stock-exchange boom. The conflicts

[52] The issue is not only that of discrimination of shareholders' (investors) rights in the framework of civil/corporate law. The criminal aspect of the problem (a threat of using force, murder, occupation of company premises by force, defense of company premises, use of law-enforcement agencies to resolve corporate conflicts) remains to be important although the authors lack data to make a by-country comparison.

widely covered by the media at that time (involving "Noyabrneftegas", "Yukos", "Yuganskneftegas", "Samaraneftegas", "Purneftegas", "Sidanko", "Nosta", "Barjeneftegas", "Chernogorneft", Vyksunsky Metalworks, Magnitogorsk Metallurgical Plant, Baltics Ship Lines, Leningrad Metalworks, "Akron", many companies in telecommunications and energy fields, etc.) signaled that the problem had become chronic and widespread. To a large extent the discussion was initiated by foreign portfolio investors that had not yet grasped the standards of Russian corporate culture. The 1998 financial crisis brought about a new wave and new instruments of ownership redistribution thus giving the discussion a new impetus. The situation developed as a result of strengthening of the positions of managers and the arrival of new shareholders who managed to buy out blocks of shares at cheep prices in the post-crisis period.

Although corporate governance of the late 90s has a negative image, in 2000-2001 effective corporate governance became one of the most widely discussed topics at dozens if not hundreds of conferences and symposia in Russia. Biggest corporations which 2-3 years ago were known as hard-core violators of shareholders' rights urgently adopt "codes of corporate governance", set up department of "shareholder relations", bring in "independent" directors to the boards, make effort to ensure "transparency". The Federal Securities Commission developed its own "code of corporate behaviour" that has an uncertain status and purpose given the presence of the law "On Corporations". In 2000-2001 some private organizations offered to the market their own competing "ratings of corporate governance". Bureaucrats have learned how to operate the term and are turning it into a new bailout fetish.

The epidemic proportions of the passion for corporate governance have several reasons. First, at the moment the government has been left with a narrow set of tools to demonstrate activity in the area of institutional reforms. Second, for the Western institutional investors corporate governance is an idee fix from the "wild" 90s embodied in recommendations by the international financial organizations. Finally, the largest Russian issuers (what is most important) finalize consolidation of share capital using the opportunities opened after the 1998 crisis. Besides, expansion and formation of new integrated structures (groups) demanded additional resources while formal standards of corporate governance became an essential prerequisite for creating a conflict-free image of reorganization programmes and getting access to the external (foreign) sources of investment.

The 2002 survey by the Association for Protection of Investors' Rights showed that assets stripping and transfer pricing are the most typical violations of shareholders' rights (39 % of the respondents) followed by intentional and fictitious bankruptcy (20 %), dilution of shareholder's stake (20 %), and non-payment of dividends (17 %).[53] However, shareholders face the same risks in many countries: Indonesia, Republic of Korea, Brasilia, Mexico, Argentina, Turkey, Czech Republic, India, and others (Table 3).

Table 3. Main risks of corporate governance in Russia

Risk	**Importance of risk in Russia in 2002 ("+++" - maximum)**	**Unique character of the risk for Russia**	**Presence in other developing economies**
"Dilution of authorized capital"	++	No (but progressing quickly before 2001)	Korea
"Assets stripping and transfer	+++	No (but wider used)	Indonesia, Malaysia, Korea, Mexico

[53] See: www.corp-gov.ru.

pricing"			
Information disclosure	++	Yes (but much worse that in other countries)	-
Reorganization (mergers and takeovers)	+++	No (but conditions are often arbitrary and non-transparent)	Malaysia, Корея, Indonesia
Bankruptcy	+++	No (but often used as a means of takeover or asset stripping)	Practically everywhere
Managers' behaviour	++	No (but for inadequate perception of corporate governance is characteristic of many companies)	Many examples in various countries
Limitations to share ownership and using the voting rights	+	No (in Russia the limitations are relatively rare)	Korea, Mexico, Thailand
Registrar	+	No (rare cases in the recent years)	India (partially)

Source: Brunswick Warburg and authors' re-eveluation.

The second myth reflected by many evaluations is that Russia lacks a developed corporate law. Although elements of law specific of the transition economy and wide gaps do exist (see p. 3.1) the effective Russian legislation in the area can be viewed as highly developed from the point of view of the presence of formal universally accepted measures aimed to protect shareholder rights (Table 4). At the same time, real problems of corporate governance in Russia should be evaluated from a different angle (see p. 3.2.2):

- economic limitations and contradictions in forming a national model of corporate governance
- presence of legal forms of violating shareholder rights (within the framework of the law "On Corporations", other acts) that have emerged and are widely used due to the imperfection of the legislation and unambiguous interpretation of its norms;
- specific character of law enforcement.

Table 4. Comparative by-country analysis of shareholder rights

Shareholder rights	Positive (+) or negative (-) effect	G7 countries	15 largest emerging markets	Russia
1. One share – one vote	(+)	None	Malaysia, Greece, Chile, Republic of Korea	Present
2. Voting by post (by ballots)	(+)	Great Britain, USA, France, Canada	Argentina, Republic of Korea	Present
3. Lack of blocking of shares before voting	(+)	Japan. Canada, USA, Great Britain	Brasil, Chile, Portugal, Republic of Korea, Phillipine, Indonesia, Malaysia, Thailand, Индия, Turkey, South Africa	Present
4. Cumulative voting	(+)	Только USA	Thailand, Argentina, Phillipine, Taiwan	Present
5. Minority's right to revoke to overrule management's decision	(+)	Great Britain, USA, Canada, Japan, Germany	Argentina, Brasil, Chile, Phillipine, Malaysia, Taiwan, Thailand, India, South Africa	Present

6. Minority right to compel the majority shareholder to purchase his shares from him at an equitable price in case of large transactions, reorganization or changes in constitution	(+)	Great Britain, USA, Canada, Japan, Germany	Argentina, Brasil, Chile, Phillipine, Malaysia, Taiwan, Thailand, India, South Africa	Present
7. Percentage of shares needed to convene an extraordinary shareholders' meeting	The less the better	1 – USA 2 – Japan 5 - Canada and Germany 10 – Great Britain and France 20 – Italy	1 – Chile 3 – Taiwan 5 – South Africa, Greece, Argentina, Brasil, Republic of Korea, Portugal 10 – India, Malaysia, Indonesia, Turkey, Phillipine 20 – Thailand 33 – Mexico	10
8. Mandatory payment of dividends	Compensation mechanisms in the countries of continental law (+ for the latter)	None	Chile – 30 % Greece – 35 % Brasil – 50 % Phillipine – 50 % Portugal – 50 %	None

Sources: IKPU, 2001; La Porta, Lopez-de-Silanes, Shleifer, Vishny, 1997.

Undoubtedly, Russian company legislation (corporate lawl to be more precise) contains a considerable amount of borrowed English-American mechanisms of shareholder protection. It will be shown later that such borrowings resulted in more problems than produced positive effects. In a certain sense it would be proper to talk about the approach being absolutized (as a consequence of implementing the "self-enforcement" model) and its artificial transposition on the general evaluation of the national model of corporate governance. However, such a generalization would be wrong.

Common traditions of the European corporate law still dominate the scene which explains why the shareholder legislation in Russia is close to the EU acts standards by formal criteria reflected in the EU Regulations and Directives (Table 5). This equally applies to the standards developed by various European associations representing the private sector. [54]

Table 5. Availability and degree of development of basic legislative norms concerning companies in the Russian corporate law and EU acts (degree of development of the relevant provisions in the EU acts serves as the basis for the comparison)

Норма	Russia *	EU**
Rigid and detailed procedure of establishing corporations	Available (CC, LC)	Available (D 1, D 2), C. on EEIG 1985, and R on SE 2001
Rigid and detailed procedure of maintaining authorized capital	Available (LC, SML)	Available (D 2)
Regulation on establishing subsidiaries, representative offices	Available (CC, LC)	Minimum (D 11 in the area of accountability)

[54] See: EASD, 2000; Euroshareholders, 2000. For detailed comparison of pan-European codes of corporate governance and the EU Member States codes see: Weil, Gotshal and Manges LLP (2002):

and other autonomous		
Main issue of reorganization	Available (CC, LC) but provision of further detail is needed for: reorganization forms measures to protect rights of shareholders and creditors	Available (D 3, D 6, draft D 10 on cross-border)
Control over "economic concentration"»	Available (CLMA) but not efficient	R. on mergers, 1989
Possibility of a single-member company	Available (LC)	Available (D 12) For close/private companies
Pre-emptive right of shareholders to buy out shares	Available (LC, Amendments of 2001)	Available (D 2)
Choice between one-tier and two-tier management systems	Available (LC)	Available as a compromise on national models (draft D 5, R. and D. of 8 October 2001 on SE)
Employee involvement in management	Not available	Available as a compromise on national models (draft D 5, R. and D. of 8 October 2001 on SE))
Stringent requirements towards financial reporting and audit	Available (SML, LC, and others) but it is still necessary: to relate the degree of toughness to the company size; to create conditions for switching over to international standards	Available (D 1, D 4, D 7 on consolidated financial reports, D 8 on audit, D 11)
Takeovers and protection of minority shareholders	Available (LC) but further elaboration is needed	General principles at the discussion stage (draft D 13) due to conflicts of national approaches
Company groups (groups of enterprises)	Minimum and contradictory on subsidiaries and dependent companies (CC, LC), "group of persons" and affiliated persons (CLMA)	Minimum (D 7 on consolidated accounts, social aspects, draft D 9 on "group behaviour")
Bankruptcy	Available, but a radical modification of legislation is needed	Minimum (C. of 1995), mainly regulation of inter-country collisions
Insider deals	Minimum, a special law is needed	There is a direct ban and minimum standards(D.)
Liquidation	Available (CC, LC)	Not available

** LC – law "On Corporations", CC – Civil Code of the RF, SML – law "On Securities Market", CLMA – law "On Competition and Limits to Monopolistic Activities on Commodity markets"; ** D – Directive, R – regulation, C – Convention.*

No serious problems should be expected if there is a need formally bringing the Russian corporate legislation in line with the EU norms (if one leaves aside the political oppositions in Russia and the EU that use various excuses).

3.2.2. Real criteria and recommendations for Russia

A) Russian problems

The following key features of development of the Russian model of corporate governance should be mentioned:

- permanent process of ownership redistribution in corporations;
- specific interests of many insiders (managers and big shareholders) related to control over financial flows and assets stripping;
- weak or untypical role of traditional "external" mechanisms of corporate governance (securities market, bankruptcies, corporate control market);
- substantial government stake in share capital and the ensuing problems of management and control;
- federal system of government and the active role played by regional authorities as independent subjects of corporate relations (the subject acting under the situation of conflict of interests as owner, regulator, business actor);
- ineffective or/and selective (politicized) law enforcement (with relatively well developed legislation on shareholder protection).

The above features have been given an extensive coverage by the domestic literature.[55] At the same time, the very fact of a discussion about "corporate governance" at least when a large corporation is in question can be justified only if the processes providing its economic basis are in place: separation of management from ownership; separation of finances (certain sources of finance) from management.

Besides, when discussing about what type of financial system should be favoured it makes sense to the discuss structure and the level of concentration of share capital which define the forms of exercising the right of control in a corporation. Some others take the view that under the modern conditions the legal approach (legislation and enforcement) is more suited for understanding corporate governance and its reforms than the conditional division of bank and market-oriented financial systems.[56] Put differently, a question arises about the counter-effect of law on development of economic prerequisites of the emerging model of corporate governance.

The following processes of principal importance for the prospects of development of the Russian model of corporate governance can be identified[57]:

- latent situation with the process of division between ownership and management (merger of "controlling shareholders" and "managers") will persist in the mid-term;
- probability of widening in the next few years of the external finance as the second prerequisite for effective management is extremely low;
- Russian financial system in its present indeterminate form does not allow making even a preliminary evaluation of to what extent the Russian system of corporate governance leans

[55] See papers by S. Aukutsionek, M. Afanasiev, I. Belikov, D. Vasiliev, T. Dolgopyatova, B Kuznetsov, R. Kapelushnikov, A. Klepach, P. Kuznetsov, G. Malginov, Y. Mirkin, A. Muraviev, A.Radygina, Y. Simachev, I. Khabarov, R..Entov, A. Yakovlev et al.
[56] See: La Porta, Lopez-de-Silanes, Shleifer, Vishny, 2000.
[57] For more detail see Radygin, 2002.

to the classic models (first of all, to other - beside self-financing – types of sources of finance and, consequently, control);

- nevertheless, concentration of share capital is an obvious process which covers not only consolidation of control, but also realization of the "self-financing" model of corporate governance (proposed for the transition economies in the mid-90s within the enforcement context);
- legislative innovations in the field of corporate legislation as such (shareholder protection) in a certain sense have reached their limits from the point of view of the existing conditions;
- methods of shareholder protection can not be developed further without adequate general measures in the area of enforcement;
- methods of monitoring managers will remain ineffective in the absence of a well-developed system of competitive commodities markets, capital and labour markets, bankruptciesбанкротств.

Besides, in 2002, taking into account a long list of empirical and legal data, it is reasonable to talk about the stable and fundamental collision within the emerging system of corporate governance. It stems from the fact of coexistence of two contradictory approaches within the established system (Table 6):

- concentration of share capital that implies minimum of legal shareholder protection mechanisms;
- Anglo-Saxon legal tradition characterized by maximization of mechanisms of legal protection of minority shareholders (connected to a considerable extent to the designers' ideology but adopted piecemeal because of the fierce opposition).

Table 6. Comparative characteristics of national models of shareholder protection *

	(1) German and Scandinavian model	**(2) Countries of common law**	**(3) Countries of French civil tradition (most widely spread)**	**(4) Russia**
Formal concentration of shares with 3 top shareholders in 10 top private corporations (average for 49 countries - 46 %)	34 (Germany), 37 (Scandinavia)	On average - 43 (USA – 20, Great Britain, Australia – below 30)	54	By the 2001-2002 data intermediary between (1) and (2)
Legal mechanism of investor protection	Average	Best	Least effective	Formally close to the common law countries
Level of law enforcement	Highest	High	Lowest	Can not be compared

Originally comparison was performed for (1), (2) and (3) without taking account Russia and other transition economies. High standards of accounting, legal mechanism of investor protection and enforcement level very negatively correlate with ownership concentration. Undoubtedly, certain limitations of the survey should be taken into consideration: only top 5-10 companies with the highest capitalization were reviewed in every country, only nominal ownership was considered (not the aggregate of control mechanisms), etc..
Sources: La Porta, Lopez-de-Silanes, Shleifer, Vishny, 1997, pp. 32-35, 40-43; for Russia – the authors estimates.

Their combination resulted in a unique situation of mutual neutralizing:

- on the one hand, concentration of share capital and gradual "crowding out" of small shareholders in principle diminishes the importance legal mechanisms of share holder protection from the point of view of the corporate sector as a whole while the mechanisms themselves are being transformed into mechanisms of corporate blackmail;
- on the other hand, the development of a comprehensive network of shareholder protection impedes the process of share capital concentration (as a factor of a counter-effect of law on economic processes).

It should be taken into account that protection of interests through further concentration is the prerogative of large shareholders, their reaction to lack of legal mechanisms of protection and, first of all, to "contract enforcement". This process is not directly related to the problems of minority shareholders who have neither consolidation means nor judicial privileges.

Surveys data show that the largest shareholder's stake in Russian companies changed slightly in 1999-2001 and amounted to about 30-35 % while the stake of the 3 top shareholders – to about 40-45 %. It might be assumed that the average level of concentration has reached its formal threshold – within the framework of the effective corporate legislation (corrected for the antimonopoly regulation and formal requirements towards takeovers).[58]

More optimistic interpretation shows that by 2002 a "model" balance was reached between the level of concentration (corrected for the relationship of affiliation and alliances) and a certain set of measures aimed to protect small shareholders. The element of optimism lies in the fact the system has reached a certain degree of stabilization. The problem is presented by the fact that it has begun to reproduce itself because of the mutual neutralizing of the key components described above.

Paradoxically, by virtue of this contradiction, within the framework of the discussion about convergence of the continental and English-American corporate models Russia finds itself in an advantageous position.

That is why the issue of availability of economic and institutional preconditions for gravitating to one of the classical models of corporate governance acquires great importance.

The model characterized by domination of the interests of small shareholders (or with a sharp focus of the legislation on absolute protection of small shareholders) apparently is not as impossible as impractical. Realization of such a model, to a considerable extent based on the Anglo-Saxon practice, precedent law and ideas of self-sufficiency of corporate law in Russia (the mid-90s) would require a serious economic overhauling of the established relations (although at the same time it is hard to agree that such relations are beneficial). A sharp bias in favour of minority shareholder interests shatters the balance of interests of all the rest of the subjects of corporate relations who have an equal right to be protected from the point of view of the general principle of protection of ownership rights. Nevertheless the role played by small shareholders is of critical importance for ensuring company transparency.

Note that inadequate legal protection of (small) shareholders and the relatively low level of the securities market development are likely to be interconnected in a direct and an inverse ways: liquidity of many shares at less developed markets makes their holders still less protected which in its turn fosters concentration of corporate ownership and reduces market mobility of the shares.

[58] In the USA in 1984-1990 the stake of the biggest shareholder in companies with various types of ordinary shares was 32 %. (Zingales, 1995). The stakes of 3 top shareholders in 10 largest corporations of 49 countries were on average 46 % (La Porta et al., 1997.).

Moreover, it could be argued that in Russia (in spite of the above contradiction in the approaches) an objective (by its economic reasons) gravitation towards the European model of corporate legislation is taking place. This conclusion is based on similarity of the key problems facing Russia and the continental EU Member States.

As K. Hopt mentions, the original conflict in terms of "principal-agent" in the European company legislation is not a conflict between shareholders and the Board of Directors (which, in accordance with the American tradition of the 30s, is the most widely discussed in the framework of the modern economic theory[59]), but the conflict between majority and minority shareholders (Hopt, 2000). The situation is based on the differences between Europe on the one hand and the USA and Great Britain on the other in the area of corporate ownership and control structure that make it possible to identify two different types of corporate governance systems – insider and outsider systems. In the USA and Great Britain neither private shareholders nor institutions have a considerable stake in corporations. On the continent shareholder ownership is highly concentrated in the hands of families, other big companies or universal banks (the "groups" phenomenon). Reciprocal and cross holdings are also widespread. In such companies Boards are often nothing but puppets in the hands of the controlling shareholder or the parent company. European company law reacts to this challenge (if it does this at all) by offering various measures aimed to protect minority shareholders.

Apparently, Russia finds itself in the situation typical for the continental "insider" model with puppet Boards of Directors. Of less importance is the difference in the area of enforcement. Although, as mentioned above, there are also serious differences between the Western countries (Table 6) a reform in this area in Russia is most urgent (see also Radygin, Entov, 2002);.

In the long term, the world tendency towards approximation of the corporate governance models (mutual borrowing of various components and mechanisms, i.e. not as much a one-way borrowing as convergence) should be taken into consideration. In certain sense this confirms the point of view that by itself legal formulation of the model of corporate governance (legal instrument) is of secondary nature and based on real economic processes, including the global ones.

In general, it is obviously necessary to move in the direction of a certain mixed model that will take into consideration the principles and tendencies described above and at the same time offer a balance of interests of all the shareholders and the "stakeholders".

In practical terms it means that at this particular moment of time legal formulation of a "national model" of corporate governance that would correspond to any of the classical standards (that become increasingly blurred themselves) is not expedient (possible). The key task from the view of the state should be reviewing corporate governance in the context of protection and guaranteeing ownership rights (rights of investors and shareholders) and ensuring a balance of interests (rights) of all the participants in corporate relations. [60] Corporate governance as an essential institutional precondition of economic growth should be considered exactly in this context.

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[59] In particular, emphasis is made on how company legislation can compel directors to be more responsive to shareholder interests. Normally such reforms do not take account of the Board structure (whether it is one-tier or two-tier) but instead focus on such issues as the Board size, independent directors, conflict of interests, Board committees, frequency and efficiency of meetings, Board members remuneration, etc. The key problem is finding a reasonable balance between the right of making business-decisions delegated to the Board's members on the one hand, and control over them through application of structural and other legal norms and establishing a certain level responsibility on the other. Only recently a discussion has started about comparative advantages and disadvantages of one-tier and two-tier Board systems, the influence, and independence of the Board members.
Other aspects of internal control (cooperation with employees and banks' role) are also under review to a considerable degree one-sidedly depending on what country the authors are from. Arguments for and against are most often unconvincing (see also Hopt et al, 1998).

[60] See also: Radygin, Entov, 2001.

However, the fight for control over and redistribution of ownership (both by virtue of objective processes of the transition economy and due a range of subjective factors) will continue in the years to come. Therefore, creating a well-defined legal framework for such redistribution remains a priority task.

At the same time, the above considerations concerning economic limitations make it possible to suppose that a relatively long transitional period is needed to size up at least to the European formal norms of company legislation and applied standards of corporate governance.

B) EU problems and recommendations for Russia

First, the historic experience of the EU (in the area of establishing supra-national norms of company law) is evidence that the highest rates of unification were characteristic of the 60-70s while the 80s saw a marked slow-down of the process (see Asoskov, 1998). In the 60-70s unification covered first of all the norms that had already been developed at the national level (company participation in ownership turnover, guarantees to shareholders and creditors, etc.). The latter fact fostered adoption of First and Second Directives that contain very stringent provisions. In Russia, regulation in this area has been developed to a considerable extent.

In the 80s the EU governing bodies made an attempt to unify internal corporate relations (covering, first of all, structure of management bodies, employee involvement), i.e. areas where national differences are significant. To a considerable extent the problem of unification acquired a political dimension. Consequently, the nature of EU Directives has been markedly changed: they began to offer a choice among several variants (in fact, fixing the diversity of national approaches). The problem is easily traceable in the 30-year long discussion about the "European company" that resulted in 2001 in adoption of the multi-variant documents. Adaptation to the standards of the "European company" model presents no big difficulties for the Russian corporate law.

Second, a wide range of important company regulation issues (management bodies, liquidation of companies) remain outside the EU regulations. Some issues (company groups, for example) have different degrees of regulation in the EU Member States. In general, differences in company regulation across the EU remain wide.

Third, historically, law enforcement and judicial systems of the EU Member States differ significantly (see Potemkina, 2001). Correspondingly, one of the main areas of activities identified in the Amsterdam Treaty is to define the framework of the "European legal space", i.e. to ensure efficient implementation of the conventions related to civil and criminal cases, equal opportunities for all to appeal to court, quick and efficient performing of judicial procedures. The Extraordinary EU Summit in Tampere (October 15–16 1999) re-confirmed that the presence of 15 different national judicial systems impedes the internal market development, restricts the freedom of movement of the EU citizens and their freedom to engage in professional activities. This is why in order to implement the idea of the European space of freedom, security and legal protection the Treaty of Amsterdam envisages strengthening of cooperation between the EU Member States in the area of the "third pillar" and its partial "communitarization", i.e, bringing some territorial law and judicial provisions to the supranational level.

Fourth, the general approach to the strategy of company law unification within the EU remains controversial. In particular, there is the idea that unification of all the areas of the company law is not needed. Some researches (see Harm-Jan de Kluiver, 1996, p. 86) hold the view that it would be enough to carry out harmonization in the area of protection of the rights of shareholders and stakeholders in general which was originally envisaged by the Treaty of Roma.

The following issues mentioned above remain to be important topics of the discussions within the EU:

- the "XXI century corporation" and its standards,
- expediency of orientation towards the English-American model,
- role of private and institutional investors,
- outsider role in company groups,
- acceptability for the EU of certain internal (Board of Directors, employee involvement, banks' role) and external (capital market, takeovers, audit, information disclosure) mechanisms of corporate governance,
- role and effectiveness of government regulation and self-regulation systems,
- role of litigation and courts in enforcing company legislation,
- ratio between convergence and harmonization of company legislation,
- priority of company legislation reform at the ERU level.

As mentioned above, the existing problems and the quest of the EC bodies for continuation of the unification process led to setting up in 2001 of the High Level Group of Company Law Experts. Frits Bolkestein, member of the EU Commission formulated its tasks as: «This High Level Group has been set up because the Commission wants to get top quality independent advice from leading European experts in the first instance on pan-European rules for take-over bids and subsequently on key priorities for modernizing company law in the European Union. A clear set of pan-EU rules for the conduct of takeovers stands to benefit European companies and shareholders, especially minority share holders, by clarifying their rights and obligations. It would also facilitate the goal set by the Lisbon summit of restructuring the European economy to make it the most competitive in the world by 2010». [61]

The problem of takeovers was analyzed above. As to modernization of company legislation (the second stage of the group activities) the most general objective is to develop a framework company legislation for the EU that would be flexible enough to meet the modern company needs and at the same time reflecting the effects of information technologies. In particular the following issues are planned to be studied:

- formation and functioning of companies and company groups, cooperatives and mutual enterprises, including issues of corporate management;
- shareholder rights, including cross-border voting and "virtual" general meetings;
- corporate restructuring and mobility (first of all, transfer of the official seat of the company);
- potential need in new legal company forms (first of all, close European Private Company that has a special importance for small and mid-size EU companies);
- possible simplification of corporate rules in view of the provisions of the report on Second Directive of 13 December 1976 (SLIM report) concerning formation and maintaining capital of public companies.

A look at the urgent problems of reforming corporate legislation in Russia reveals a lot of common features with the current problems of the EU reform in the area.

[61] http://europa.eu.int/comm/internal_market/en/company

The following first priority issues deserve to be specifically mentioned: mergers and takeovers, control over large transactions, affiliated structures, beneficiary holdings and owners' liability, company groups, bankruptcies that help retain government's stakes in the corporations. Apparently no progress will be possible if an effective infrastructure and political will to enforce legislation are lacking.

It is clear that even if the problem of Russia's accession to the EU is positively resolved a long period of transition will be needed to adapt and harmonize legal norms and standards. Nevertheless, irrespective of the progress in the process of Russia's accession, it is time already to discuss a number of positive innovations (at the level of adaptation) that are present in one way or another in the EU acts. Here are some of them:

- adoption of new norms of company legislation publicly by all the parties concerned (in accordance with the procedure set for developing Directives);
- dependence of information disclosure level (transparency) on economic conditions: company size, organization and legal forms of the company, ownership concentration (Fourth Council Directive and others);
- creditor protection and the requirement of independent valuation in cases of merger or takeover (Third and Sixths Council Directives)[62];
- regulation of employees' rights in case of company reorganization (Directive 77/197);
- development of conditions under which companies having subsidiary undertakings should be required to prepare consolidated (Seventh Council Directive), although meeting difficulties is enevitable (the Directive has not been implemented in every EU Member State);
- transparent and well-defined requirements to natural and legal persons responsible for carrying out audits (Eights Council Directive), although difficulties are to be expected with carrying out effective audits in cases of mergers of ownership and management (Russia) or with "puppet" Boards of Directors (some EU Member States);
- provision of incentives for single-member private limited-liability companies (Twelfth Council Directive), which is of particular importance under the Russian conditions considering the tendency towards closing themselves and the problem of owner liability;
- usage of proposals of Fifth Directive on cooperation with employees as recommended for companies, although in this case the position taken by a number of countries with weak traditions of cooperation (in particular, the British approach: such provisions are inappropriate within the framework of corporate law) [63];
- proposals by the High Level Group of Company Law Experts (2001) on issues related to takeover bids (see also Radygin, Entov, 2002a);
- transparence of judicial proceedings at the EU level and control by the European Court over implementation of Directives and other EU acts (see also table 7).

[62] At present the Duma and the Government of the RF review a draft federal law "On reorganization and Liquidation of Commercial Organization". The designers believe the draft is aimed to attain two main objectives – to achieve transparency and low costs of the process and the balance of interests of owners and creditors. In accordance with Third and Sixths Council Directives reorganization requires "grounds" and "valuation" for every company. It is assumed that the requirement for provision of grounds aims to protect small shareholder; valuation is voluntary. Given the problems of corporate blackmail a possibility of narrowing down of obligatory cases can not be excluded.
[63] See also: Kargalova, 2001.

In spite of the presence of other opinions it appears that the EU experience in the area of unification could be of minimum use for resolving the problem of relations between the Centre and the regions in Russia. As to applying the EU experience to harmonization of legislation within the CIS, in all probability, this is an objective of a distant future aggravated by some political problems. Nevertheless, company law that regulates the most widespread organizational and legal form might become one of the first issues of harmonization in the area of economic legislation of the CIS countries.

Table 7. Main areas of corporate management improvement[64]

Problem	Legislation in force	Improvement measures
Guarantees of registration of investor's ownership rights in company register	Law "On Securities market ", acts by Federal Securities Commission	development of standard terms of contracts with registrars selection of registrar and terms of contract with him should be subject to approval by annual shareholders' meetings registrar's liability for rules violation in case of frauds or manipulations with the register on the part of the register owners (registrars or issuers)
"Dilution" of stakes by issuing new shares	Law "On Corporations", "On Protection of Investors' Rights and Interests", standards of the Federal Securities Commission	regulation of the procedure of debentures convertible into shares provision of detailed regulation on fraction shares, especially for cases of pre-emptive buy-outs and voting at shareholders' meetings
Violations of procedures of carrying out shareholders' meetings	Law "On Corporations"	- legal clarification of ambiguous issues (for example, sending voting ballots by post to be received after the meeting should be unambiguously interpreted as a substantial violation opening the way to leave the company after receiving a compensation by a court's decision) - removal of the controversy arising from differentials in the time-schedules set for implementing various procedures in the course of preparing the meeting - regular checks of observance of the procedures of informing shareholders about the meeting and publishing its decisions (taking into account the 2001 amendments that updated the schedules)
Transfer of the vote to company management in cases of ADR and GDR	Acts by the Federal Securities Commission of the RF	Veto over issuing ADR and GDR if it involves transfer of the vote to company management
Irregularities in the process of company reorganization and consolidation	Law "On Corporations" "	- widening the list of methods of reorganization and introduction of relevant amendments to the Civil Code of the RF, the law "On Corporations", etc. - apart from meeting the demand to maintain ownership structure in case of reorganization – the necessity of a range

[64] Sources: IKPU, 2001; OECD, 2002; Radygin, Entov, Turuntseva et al., 2002.

		of measures aimed to protect creditor interests - introduction of the requirement on inviting an independent valuator - improvement of information disclosure procedures
Violation of the requirement to disclose information	Laws "On Corporations", "On Securities Market", "On Protection of Rights and Interests of Investors", standards by the Federal Securities Commission	improvement of the information disclosure legislation return to the rule of providing information to shareholders having over 10 % of the shares (under the new version of the law "On Corporations"– 25 %) ban on asymmetric provision of information to certain privileged parties and using important and closed information to gain personal advantages. - introduction of international accounting standards - introduction of criminal prosecution for failure to disclose information
Opaque structure ownership and control structure (Непрозрачная структура собственности и контроля (раскрытие структуры собственности и контроля необходимо для решения проблем возможных злоупотреблений, связанных со сделками с заинтересованными лицами, включая использование оффшорных и трастовых структур, контролируемых менеджментом или контролирующими акционерами.	Large number of acts often containing contradictory requirements (some acts are based on the share in authorized capital, others on the share of votes. Some acts take into account indirect control through nominal owners. Finally, under the effective rules there is no mandatory requirement to disclose even official agreements between the shareholders).	- consistency and conflict-free legal framework, establishing procedures and division of responsibilities between all the parties (shareholders, issuers, registrars, trustees and the Federal Securities Commission) - provision of the norm on presenting to the stock-exchange and the general public of information on changes in ownership is the responsibilities of shareholders (both domestic and foreign); - legal rules on information disclosure should cover cases of concerted actions by the parties and cases that are de facto or de jure under control of other interested parties. Sanctions for non-disclosure should be applicable in such cases too. - shareholders of PLCs are obliged to inform the issuer, the stock market and mass media on their ownership stakes to the extent envisaged by the law. This obligation to disclose ownership stakes should apply to property registered through nominal owners. Financial institutions that have the right of keeping accounts of nominal owners and registrars should be responsible for meeting the information disclosure requirement. - 3The law should also envisage adequate and clear criminal and civil sanctions for failure to provide information on significant changes in ownership. Such sanctions should be

		applicable to shareholders, issuers, registrars, and bailees.
"Assets stripping"	Law "On Corporations", Criminal Code of the RF (Articles 165, 201, 204)	- Labour legislation reform (simplification of the procedure of dismissing Director General) - improving financial reporting procedures - more detailed requirements for concluding high-volume transactions and transactions by interested parties - qualification of transactions with affiliated persons, widening of the notion of "affiliated person"», - defining the notion of a "group pf independent but economically coherent persons"
Transfer pricing	Law "On Corporations" Criminal Code of the RF (Articles 165, 201, 204)	- improving tax legislation and its enforcement - improving financial reporting
Deliberate (fictitious) bankruptcy followed by buying out of assets	The law "On Bankruptcy", Criminal Code of the RF	- making receivers responsible for taking measures (transactions with assets) in the interests of some creditor - development of legislation on disqualification of managers acting to the detriment of the company and its creditors - taking additional measures (developing criteria for initiating bankruptcy procedures) to prevent unfair ownership redistribution and opening procedures against actually solvent companies; - wider use of the practice of turning down by courts of bankruptcy procedures as a means of debt settlement (abuse of power under Article 10 of the Civil Code of the RF) - defining with higher precision the role to be played by government authorities (as creditors and as representatives of the state's interests)) in the bankruptcy procedures
Hostile takeovers through the use of administrative pressure	In respect of minority shareholders – Law «On Corporations», in respect of economic concentration – the anti-monopoly legislation	- detailed regulation of the offer, equitable price and bidding procedure; - the whole range of measures envisaged by the institutional reform
Ungrounded lawsuits (blackmail) against issuer (large shareholder)	Court practice only	- introduction of an alternative dispute settlement procedure – carrying out administrative or arbitration hearings by the state regulator, - development of the system of courts of arbitrage - development of procedures aimed to protect the Board of Directors (management) from abuse of rights of

		minority shareholders through (a) checking reasonableness of complaints, (b) usage of the so-called "safe harbour" (such means of legal protection as "business discretion" rule or rejection of groundless information disclosure requirements), (c) resolving the problem of lawsuits by the shareholder "holder of 1 share" (introduction of quotas or development of group lawsuits requirement)
Law enforcement (including the problem of the shareholder appealing to a court)	A set of legal and procedural rules	- continuous setting of precedents (for example, under the law "On Corporations" a shareholder has the right to recover in favour of the company damages inflicted by the managers. It is next to impossible to describe such damages in the legislation. Therefore, of special importance become specific court rulings) - judicial reform as a whole a set of anti-corruption measures - provision of better training in such areas as commercial law, company legislation, securities law, bankruptcy law; - training of judges in business fundamentals as lack of experience sometime results in excessively literal interpretation of the law; - studying the possibility of judges to be specialized in commercial law (establishing specialized units of courts of arbitrage dealing with corporate and securities lawsuits). - open publication and distribution of written court's rulings aimed to increase responsibility of the legal system; - development of mechanisms of private dispute settlement and of independent arbitrage (the system of extra-judicial dispute settlement - administrative hearings or arbitrage).
Limitation period on privatization dealings	Under the Civil Code of the RF - 10 years	Reduction to 3 years

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