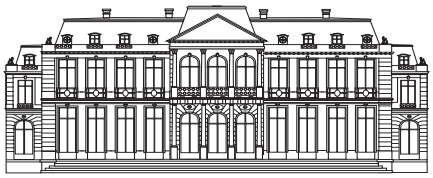
Organisation for Economic Co-operation and Development



Organisation de Coopération et de Développement Économiques

in co-operation with

the United States Agency for International Development (USAID)

and

the World Bank

Conference on

"CORPORATE GOVERNANCE IN RUSSIA"

Roy Jones
TUAC / OECD

THE MAIN APPROACHES TO CORPORATE GOVERNANCE: EXPERIENCE FROM OECD COUNTRIES

Moscow, 31 May - 2 June 1999

INTRODUCTORY REMARKS

I would like to add my voice to the previous speakers in expressing thanks to the hosts of this important conference: the OECD, US-AID, World Bank, and of course the Russian Supreme Arbitrazh Court and the Federal Commission for the Securities Market.

In preparing my intervention I reflected on the diverse ways in which corporate governance frameworks have evolved in OECD countries. I was struck by the way that in all countries, albeit in different ways and at different speeds, corporate rights and responsibilities have developed alongside and interacted with social rights and responsibilities. Similarly, I was struck by the parallel development of institutions, such as free and democratic trade unions and business organisations that are vital parts of our corporate governance landscapes, and which in turn form part of the foundations that underpin market economies. When remaining in balance these aspects have in my view helped to build and sustain democracy in our countries.

Our corporate governance history then holds valuable lessons for Russia that go beyond microeconomics, and into the broader political and social sphere as it seeks to make the transition to a market economy that benefits all in society, and not just narrow elites. The Russian government could if it chooses to adopt some of our corporate governance experiences actually be putting in place some of the necessary building blocks of democracy.

A Comment on the OECD Background Paper

In light of my opening remarks I would offer the following comments on the background paper for this opening session. In general the role of investment, financing and the financial system in corporate governance, though an important element is only part of a bigger picture, that in reality encompasses multi-stakeholders, each with rights and responsibilities. Reform efforts in many countries are not solely driven by the business sector: trade unions and civil society groups are also strong advocates here, with complementary and differing projects. While a country's institutional corporate governance framework is based around statutory law and regulations; voluntary standard contracts and self-regulation; and implicit rules, social norms and business culture, the paper is insufficiently developed as to the constituent parts of the first two elements. In practice relevant laws and regulations go beyond company law and securities legislation, to encompass labour laws and regulations, alongside those covering health, safety and the environment. Similarly, applicable voluntary standard contracts and self-regulation are more than those simply covering stock exchanges, public trading and accounting standards. The papers' narrow focus applies equally to the discussion on the reform agenda in OECD countries, with little attention being paid to that beyond promoting shareholder participation, and minority rights, transparency and financial information. In practice, the reform agenda is about issues around a much wider perspective, namely the "stakeholder" approach to corporate governance. It is that which this paper turns to next.

THE STAKEHOLDER APPROACH TO CORPORATE GOVERNANCE: A WIDER PERSPECTIVE

In developing the theme of a stakeholder approach to corporate governance my starting point will be the Preamble to the OECD Principles on Corporate Governance. The Principles sensibly avoid any definition of corporate governance, but they do state that countries' corporate governance frameworks in part depend on the legal, regulatory and institutional environment. In addition, the Principles note the impact that business ethics, societal, community and environmental interests have on the reputation and long term success of an enterprise. This highlights an important point that corporate governance frameworks have to balance the different and at some times competing interests of a broad range of actors - or stakeholders that combine to determine the success or otherwise of an enterprise.

This view of an enterprise goes beyond the narrow shareholder model, whose objective is to maximise shareholder wealth. The new stakeholder view has an impeccable pedigree based on orthodox economics. Stakeholders are those who have contributed firm specific risk-bearing investments, and as such have a right to the "economic residual" generated by the enterprise, and for some, but not all, a voice in the development of the enterprise. After all, that is what the shareholder model is about. So, for example, workers contribute firm specific investments, in for example work place training. On this basis suppliers, customers and creditors also contribute firm specific investments, though come below employees in the ranking of whom should have a voice in the enterprise.

On these terms corporate governance then becomes about finding ways in which to elicit long term stable investment by these stakeholders. Now, in practice as we have heard there is no one single model of corporate governance across the OECD, nor as would be expected in non-OECD countries. Moreover, and developing this theme the view that corporate governance systems fall into 2 competing camps, shareholder or stakeholder models is erroneous. While superficially attractive this is a false distinction, in that it suggests that corporate governance is a zero sum gain where gains for one group (say shareholders) come at the expense of another (say workers) in a company. Rather, the stakeholder model refines and extends the shareholder model, as opposed to being a substitute. Thus, shareholders are stakeholders, and that moves to increase value for them *requires* that other stakeholders' needs be given equal attention. Best performing companies recognise that simple truth. Furthermore, and in practice those countries that are said to most conform to the shareholder model - US, UK both display strong stakeholder characteristics, even if some commentators have yet to realise that.

As previous speakers have highlighted, there is a reform trend in many OECD countries to assign more emphasis to shareholder values. But what is striking is that, in the overwhelming majority of cases, these reforms complement, not replace, the existing systems – they are bolt-ons. This is important to remember as stakeholder type systems vastly outnumber those that are said to conform most to the shareholder model across the OECD.

Those insights should not be forgotten.

There is also a paradox here. While many OECD governments are moving to adopt elements of the shareholder model, companies themselves are increasingly recognising the legitimate interest of stakeholders in corporate governance. Under pressure from trade unions and environmental groups, these enterprises, for the most part multinationals are introducing corporate codes of conduct

covering social norms such as freedom of association and collective bargaining rights for trade unions; the banning of child labour, forced labour; and environment and consumer norms. Not just for their own direct activities but for their suppliers and subcontractors often in third countries. That, however, should not be taken as a signal that governments should further “privatise” their responsibilities over corporate responsibility. Genuine corporate codes of conduct developed with trade unions, rather, should be seen as an additional tool to hard regulation covering corporate responsibility.

The OECD itself is undertaking a Review of its Guidelines for Multinational Enterprises – an initiative, that compared to past practices, may just prove to be the most radical since their inception in 1976. And, lest we forget, the OECD Principles on Corporate governance contain a stakeholder chapter that states "“The Corporate Governance framework should recognise the rights of stakeholders as established by law”, and furthermore, that the same framework “should assure” that these legal rights are respected.

That is both a recognition by the 29 Members of the OECD that stakeholders are at the heart of corporate governance, and an acceptance that those legal rights must be upheld. This leads me on to the role of trade unions in corporate governance.

TRADE UNION RIGHTS AND THEIR ROLE IN CORPORATE GOVERNANCE

In practice the rights and role of trade unions in OECD corporate governance systems differ, dependent on each country's legal and institutional framework. In some countries they have legal rights to co-determination to directly represent employees in a company's supervisory board. In other countries where co-determination exists and where they do not have a legal right to representation, they are for the most part chosen to do so by employees through the democratic process. Thirdly, custom and practice frequently ensures that trade unions speak on behalf of workers when boards of directors or managers determine new directions for company policy. Why should this be so?

1. Firstly, the evidence is clear, trade unions are a positive force for economic development. Companies that recognise and bargain with trade unions invariably enjoy higher productivity, speedier diffusion of new ideas and technology and have better and more equitable training systems.

2. Secondly, they reduce transaction costs for firms in a range of areas and reduce negative externalities through the bargaining system.

3. And important for Russia - free democratic trade unions are vital to overcome corruption, and play a key role in building society-wide democratic institutions – witness South Africa, for example.

Turning to emerging trends, we can see that corporate governance systems and the role of trade unions therein are evolving. But, the view that an increased tendency by governments to prioritise shareholder rights automatically means a corresponding reduction in the role of other stakeholders, including trade unions is wrong. In practice and as noted corporate governance is not a zero sum game, where a gain for one group means a corresponding loss for another. It's much more complex.

By getting beneath the headlines we can see the following. While there is a tendency to prioritise more the concept of shareholder value, reforms are being bolted onto existing systems, as opposed to replacing them. At the same time enterprises, especially multinationals are reforming their own internal governance systems to more reflect stakeholder practices. The role of trade unions is evolving in line with this, and rather than being frozen out of corporate governance, new practices are emerging to ensure that trade unions retain their voice for employees.

Trade unions in many countries where they had previously been written off are emerging as a new force based increasingly on a partnership approach to economic development. In my own country, the UK, trade unions have this year been granted the legal right to recruit and bargain, which will inevitably lead to their having a greater say in corporate governance. In Korea, some limited progress has been made to extend the legal rights of trade unions in line with ILO Conventions. Much more needs to be done, but this example highlights that progressive changes can be made even in times of economic crisis – a challenge for Russia.

The international dimension should not be overlooked. In terms of hard regulation there exists a range of European Union (EU) directives that have extended employee rights within corporate governance landscapes, for example, the European Works Council directive, or the directive on Collective Redundancies. Proposals are now being discussed to extend information and consultation rights to domestic enterprises. So called “soft” developments include of course the OECD Principles on Corporate Governance that include a stakeholder chapter.

On the basis of this my humble advice then to our Russian hosts in re-designing your corporate governance system is to avoid the froth - the headlines - and take a broad view of what’s happening in reality among OECD countries. Far from being a declining force the stakeholder model is the way of the future.