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## ***Corporate Governance***

***Do codes of Corporate Governance really improve board effectiveness in continental European countries?  
Empirical evidence from the Belgian case***

By Gifty Agboton  
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**PRELIMINARY VERSION**  
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***Do codes of Corporate Governance really improve board effectiveness in continental European countries?  
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**Abstract:** The article points out the advantages of a more contextual methodology in governance research and board of director's studies. It raises in the first place the issue of board effectiveness in its main missions: the

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oversight and strategic roles, making a careful distinction between actual and perceived – from the outside – effectiveness. The authors are led to conclude that governance codes – the Belgian one not being an exception – address only superficially the strategy issues and seeks mainly to improve perceived board effectiveness. The second part of the article is an empirical analysis of the Belgian Corporate Governance Code (BCGC). It addresses its effectiveness through the examination of both the commentaries received from the public consultation and the compliance declarations of listed companies. The findings appeared to be disappointing given the fact that the Code elaboration process did not allow for consideration of the peculiarities of Belgian companies' governance system (holding companies, ownership control, board structure and composition). Ignoring the request from most companies to integrate the rights and duties of dominant shareholders in the board's structure and functioning, the authors of the Code failed to provide such companies with a solution to their main problems of governance: the agency problem between minority shareholders and dominant shareholders and the various other conflicts of interests arising from ownership control. As a result, the provisions of the BCGC which obtain the lowest degree of compliance are those related to the composition of the board and its committees, the independence of some non executive directors and of the board itself, as well as the detailed disclosure of remuneration policy. In total this initiative seems to have only little effect on the effectiveness of board.

## Introduction

In the aftermath of corporate failures and scandals at the beginning of 1990's (Maxwell, BCCI, Waste Management, Berliner Bank...), boards of directors have been subjected to an increasing pressure for greater corporate accountability. Several of these corporate failures actually evidenced boards' dysfunctions, namely their inability to maximise shareholders' value and ensure efficient decision-making and called especially into question their oversight role.

Concerns about the performance of corporations and the way they are governed led governance and business actors (shareholders, regulators, academics, practitioners) to advocate a series of governance and board reforms. They gave rise to the worldwide emergence of codes of corporate governance. Unknown in Continental Europe before the Cadbury's initiative<sup>3</sup> in 1992, codes of corporate governance have proliferated across countries as the major mode of regulation of listed corporations. They refer to a set of best practice recommendations regarding largely the behaviour and the structure of the boards and designed to address deficiencies in a country's governance systems (Cuervo, 2002, p.85; Zattoni & Cuomo, 2008, p.2). The main objectives of these codes are to increase the transparency and accountability of a country's corporate governance system for international investors and above all to improve the effectiveness, the quality and integrity of the board in large companies (Aguilera & Cuervo-Cazurra, 2004; Dieux, 2005; Wymeersch, 2005; Caussain, 2005). The priority is clearly given in these codes to the empowerment of the board because it is widely considered to have not adequately performed its oversight role. Precisely, its weakness is considered as a contributing factor of these large corporate collapses.

Despite the success obtained by codes in different legal systems, partly due to their flexibility and self-regulatory approach, the question arises as to whether they can reach their objectives and help listed companies to solve deficiencies in their governance structures. In particular, it is of interest to assess the role of codes as a way to improve board effectiveness for a twofold reason.

First, the codes of corporate governance emphasize mostly the control and monitoring role of board and focus on issues of board structure, composition and independence to hold managers and directors accountable to shareholders. By relying on "demographic" variables (variables related to board composition and structure) all removed from the actual actions of boards, the Codes may

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<sup>3</sup> The literature pointed out the pivotal role played by the Cadbury Report's recommendations in the international Code movement.

merely aim at improving the confidence of investors as to the effectiveness of board governance (perceived effectiveness) rather than actual board effectiveness (Robert & al. 2005). In this respect, according to some scholars, behavioural dynamics of boards (board process variables) is likely to be a more reliable indicator of effective governance practices than board characteristics. Seemingly, there is little consensus in the governance literature as to the specific configuration of an effective board. It is then necessary to clarify the concept of board effectiveness itself and point out the nature of board effectiveness the Codes may enhance.

Second, the importation of practices to solve deficiencies in a governance system still requires that these innovations fit with the characteristics of this system (Aguilera & Cuervo-Cazurra, 2004). The adoption in Continental Europe of governance rules designed according to Anglo-Saxon tradition, and particularly to what is considered best practice in the United States, necessitates thus an acclimatization process of these standards to the Continental specificities. The choice of soft law based on 'comply or explain' approach and public consultation are the leading means to achieve this goal. However, we contend that the success of these processes, and then the ability of the codes to enhance governance practices in Continental Europe, hinges on the reasons behind their adoption (efficiency and legitimacy arguments). If legitimization reasons prevail, as it is the case in most European Countries (Zattoni & Cuneo, 2008), the codes issued are less likely to address the country's governance problems and particularly help companies to improve the effectiveness of their boards. Our analysis of the Belgian Corporate Governance Code (BCGC) and its elaboration process aims to investigate this hypothesis and examine the code's success. Contrary to most studies related to the evaluation of the success of national corporate governance codes in Europe, (Conyon & Mallin, 1997; Dedman, 2000; Dahya & al. 2002; Alves & Mendes, 2004; Fernandez-Rodriguez, 2004; Werder & al. 2005) we are not solely concerned with the degree of compliance with best practices recommendations. We also address the question as to whether the choice of self-regulatory instrument can suffice to promote effective change in corporate governance practices that enhances firm value and account for specific business practices. First of all, we will discuss in the next section the concept of board effectiveness proposed in the literature and outline its determinants.

### **Board effectiveness and codes of corporate governance**

In their attempt to model how to assess the effectiveness of board as decision-making group, Forbes & Milliken (1999) set forth two criteria: board task performance (control & service roles) and board cohesiveness. Accordingly, board effectiveness can be defined as its ability to perform both control and service or strategic functions and to continue working together. However, according to these authors, it has proven difficult for researchers to assess the effectiveness of board in fulfilling the performance task, particularly the strategic role, in ways that is reliable and comprehensive due to the high degree of secrecy and interpretive nature of board activity. *De facto*, it is the importance placed on each role (or both) within academic and normative literature that provides an indication of the determinants of board effectiveness and thus the nature of board effectiveness. In order to assess board effectiveness, a lot of researchers and practitioners, denied a direct access to board process and strategic issues, have focused on its control role and more visible variables pertaining to board 'demography'.

Before coming to the point of board effectiveness, it will be of use recalling briefly the way in which the dominant governance literature has been framing the issue of board's duties. The precursory work of Berle and Means (1932), has provided a basic conceptual framework aimed at analysing and evaluating the governance structure of organisations characterized by separation of what they for the sake of brevity respectively called 'ownership' (compact formulation for a complex set of 'residual claims') and 'control' (right to allocating resources and concluding contracts). Separation gives rise to a potential conflict of interests between 'owners' and people entitled to the control

rights, conflict that has been modelled in the so called ‘agency theory’. In a referential work, Fama and Jensen (1983a) have complemented and in some respects corrected the framework designed by Berle and Means. In behavioural terms, the authors distinguish four steps in the corporate decision process: *initiation* – formulating proposals for resource allocation and structuring of contracts; *ratification* – choice of the initiatives to be implemented; *implementation* – execution of the approved courses of action; *monitoring* – measurement of the performance of the agents and implementation of rewards. Initiation and implementation constitute the *decision management* and are both allocated to the same agent or group of agents (the executive management), when ratification and monitoring constitute the *decision control* which is the logical prerogative of the owner(s) who is (are) the residual risk bearer(s)<sup>4</sup>. In some types of organizations, especially large public corporations where residual claims are diffused, the so called “property rights” cannot be efficiently exercised by shareholders who will delegate decision control to a board of directors. As stated at least implicitly by Fama and Jensen, the duties of the board of directors do not consist only of monitoring tasks but also of formulating the strategy and general policies of the company.<sup>5</sup> This view comes into conflict with the emerging claims on “managerial autonomy” with respect to strategy and general policies, based on the argument that in many cases executive managers exercise *de facto* a significant part of the residual rights of decision making. This latter view is thus restricting the prerogatives of the board to monitoring.

The control role of board is at the centre of agency theory and refers to the board’s (legal) duty to monitor and discipline top managers in the interest of residual claimants, generally restricted to shareholders. In the view of agency theory which has placed the board in the core of the corporate governance debate, board is obviously a control mechanism and board effectiveness is presumed to be a function of its independence from and tight control of management (Roberts & al., 2005). Board effectiveness in fulfilling this role has then been measured by ‘demographic’ variables such as board composition (proportion of outside or independent directors in the board, managerial experience, age, tenure of board members, etc.) and board structure (division of labour between the board chair and the CEO, board size, board committees, etc.) Finkelstein & al. (2009). Most studies in governance and board literature testing the efficacy of board governance and firm performance have relied on these demographics variables. Nonetheless, as noted by the same authors in their recent review of literature, much of the empirical studies have produced mixed and inconsistent findings, shedding doubt on the efficacy of agency theory and its associated prescriptions as regards board of directors. The main reason is that these objective variables, advocated also by alternative theoretical perspectives, are all removed from the actual actions of boards and then merely condition board effectiveness. They represent indeed proxies for board effectiveness but do not reflect the nature of effective board functioning since they let aside the complexity of how boards work. Besides, research on boards seems to be undermined by the inadequate attention to the role of some intervening processes between board characteristics and both board-level and firm-level outcomes (Forbes & Milliken, 1999). Scholars contend that, without direct measures of working processes and effects of boards, it is difficult to determine the actual level of their effectiveness in fulfilling and promoting their two roles. Furthermore, the control model dominant in the corporate governance debate has

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<sup>4</sup> Justifying the assertion that all the control rights ought to be allocated to the residual risk bearers is beyond the scope of the present paper. The most common justification, though questionable, is that this governance structure is the efficient solution to the at least potential conflict of interests between the more or less distant owner(s) and the management [see among others: Fama & Jensen (1983b)]. When the mainstream of the literature is contending that shareholders are the only residual risk bearers, a growing number of authors argue that other stakeholders, and always at least part of the salaried workers [see e.g. Blair (1995)], are or may be in this position. This latter view is reflected in French and German Company laws, which expressly state that the fiduciary duties of the board are not only to shareholders but to the company itself as a legal person consisting of a complex “nexus” of residual rights.

<sup>5</sup> As mentioned explicitly **since 2002** in the Belgian Company law (art. 524bis)

deterred analysis of board members as strategic actors and created, according to Roberts & al (2005), a tension within boards between their role of control (preserve of non executive directors) and their strategic role (preserve of executive directors<sup>6</sup>). In an attempt to really understand the factors that contribute to actual board effectiveness, researchers and practitioners have increasingly called for more theoretical pluralism and significant attention to be paid to board processes and dynamics. Answering to this call despite the difficult access to pertinent information, a growing part of the literature on governance has devoted a renewed and substantial attention on strategic issues and clearly favoured a more active role of boards (beyond mere control) in companies.

Although the literature is only just starting to examine (theoretically and empirically) the behavioural dynamics of boards and its impact on board outcomes, interesting and valuable findings are available already (Forbes & Milliken, 1999; Pettigrew & McNulty, 1999; Roberts & Stiles, 1999; Stiles, 2001; Roberts & al. 2005). In their theoretical model of board dynamics, Forbes & Milliken showed that board effectiveness in fulfilling its two roles is likely to depend more on some critical board processes rather than board characteristics. They identified three board processes related to group participation and interaction, the exchange of information and critical discussion: effort norms, cognitive conflicts and the presence and use of knowledge and skills. The authors also described how these processes enable boards to carry out the effective oversight of organisation and contribute effectively to corporate strategy. Finally, they showed how the study of board processes can help understanding and sorting out the inconsistent findings of empirical studies mentioned above<sup>7</sup>. Some empirical studies based on primary qualitative data have also explored the inner working of the board and proposed valid and reliable measures of board effectiveness in line with those identified in Forbes & Milliken's model. For instance, Roberts & al.'s (2005) based on forty in-depth interviews with UK directors focused on accountability<sup>8</sup> as a central concept in the explanation of board effectiveness. It refers to the ability of boards to hold management accountable for present and future actions and is achieved through a wide variety of behaviours that are at the centre of how board's members seek to be effective: challenging, questioning, probing, discussing, testing, informing, exploring, encouraging, etc. Some of these behavioural factors have been outlined in others studies as contributing to efficient decision-making and board performance (Stiles, 2001; McNulty & Pettigrew, 1999). According to Roberts & al, it is the ability of board members to create and sustain accountability within the board in relation of both strategy and performance that determines actual board effectiveness. In this view board effectiveness can be defined as the extent to which boards are more active and involved in the strategy of corporations, in the sense that they effectively participate and influence the non-routine decisions processes that take place at the highest echelons of the firm and have the potential to affect the direction and performance of the firm (Judge & Zeithmal, 1992; Forbes & Milliken 2009). By highlighting the criteria and conditions of effective board functioning, this emergent literature appears to be relevant with respect to governance practices and has some implications<sup>8</sup> in terms of boards' reform as it was the case in UK with the Higgs Report. Actually, these findings underscore the need for practitioners and policy-makers to be informed by an understanding of board processes and adopt process-related measures to efficiently enhance board functioning (Forbes & Milliken, 1999, Roberts & al.2005). Governance reform, argued the latter, must seek both to enhance the effectiveness of the direction and control

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<sup>6</sup> In a growing number of listed companies this role is effectively assumed by the "executive committee", while the sole CEO is a member of the board and thus the only one to be responsive to the board.

<sup>7</sup> The board demographic variables may not improve board functioning because of the multiple and contrasting effects that they are likely to have on the processes that contribute to effective board performance: while the proportion of outside directors in board can enhance effort norms and cognitive conflicts, it can also reduce the presence of firm specific knowledge and board cohesiveness.

<sup>8</sup> Here the use of the term 'accountability' is different from the traditional conception of accountability in the corporate governance debate where it is equated with monitoring and controls (remote accountability). It refers to the face-to-face accountability within the board between executive and non-executives (Roberts & al).  
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of companies (actual board effectiveness) and to create confidence in distant investors as to the effectiveness of what goes on in boards (perceived effectiveness).

Unfortunately, recent academic advances examining the actual actions of boards and the factors central to board effectiveness do not appear to be reflected in current governance reform based on the codes (Nicholson & Kiel, 2004). Driven by the basic concern to improve current practices and avoid further scandals, many governance reforms have adopted a narrow view of governance emphasizing the reporting and control roles of boards at the expense of a vital function, their strategic role<sup>9</sup> and henceforth focused largely on structural governance issues. Pursuant to the prescriptions of agency theory, board are expected to play an independent role as regards the oversight of management through three key measures: the splitting of chairman and CEO roles, the increase in the number of non-executive and independent directors and the creation of board subcommittees in areas where conflicts of interests are most likely (audit, remuneration, nomination committees). The codes' rules are intended to improve the working and the quality of the board in order to hold managers accountable for their actions and increase transparency and accountability of companies to shareholders. Precisely, for investors or academic researchers, denied a direct view of the work of the board, the codes' rely on structural aspects of board governance that are presently deemed appropriate and adequate proxies for board effectiveness (Useem & Zelleke, 2006). As we have discussed above however, these observable variables on which current governance practices assessments are widely built upon have limited effect on board effectiveness and may purely aim at enhancing the confidence of investors as to the adequacy of board governance must be kept in mind that most corporate reforms undertaken in the wake of corporate irregularities have not genuinely been informed by an understanding of board processes and behaviours and – except for OECD and some UK reports – have neglected the importance of board involvement in strategy and considered exclusively its oversight role McNulty & al. (2005). For instance, in the case of Belgian Code where the provisions at least implicitly refer to the strategic role in accordance with the Law, our analysis backed by some comments showed that they address the strategy issues only superficially.<sup>10</sup>

There are alternative reasons for the limited impact the codes may have on efficiency of governance practices which may explain the concerns regarding corporate governance codes as a way to improve board effectiveness. First, it will become increasingly difficult to differentiate effective from ineffective practices through a screening of structural aspects of corporate governance since all firms maintain the same structural governance standards (Schmidt & Brauer, 2006). Second, observe the same authors (2006, p.13), “within the climate of new corporate governance rules, the question arises as to whether or not boards of directors, motivated by the fear of protecting reputation and limiting liability, are now focusing too heavily on checklists and box ticking instead strategic of issues”. Indeed, innovations like the codes are seemingly isomorphic<sup>11</sup> and then tend to favour symbolic rather than actual compliance: companies are particularly prone to look to one another for ideas of what constitutes best governance practice. This point leads us to the next section explaining the reasons behind the adoption of corporate governance codes in Continental Europe and their potential effects on countries' corporate governance practices.

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<sup>9</sup> However, some codes (Cadbury, 1992; Hampel, 1998) warned against the dangers of over-emphasizing the control role of board (Roberts, McNulty & Stiles, 2005).

<sup>10</sup> Some comments regret the lack of substantial attention on boards' responsibility for key elements such as goal-setting, portfolio strategy, business strategies as well as major resource commitments and divestments.

<sup>11</sup> DiMaggio & Powell (1983) define isomorphism as a constraining process that forces one unit in a population to resemble other units that face the same set of environmental conditions (Ruigrok, Peck & Keller, 2006, p.1209).

## Diffusion of corporate governance codes in Continental Europe: competing hypotheses

As codes of good governance spread across countries with different economic organisations and legal systems, the governance standards require substantial adaptation (we called it 'contextualisation') to be applicable to the wide range of company profiles in European markets. Board functions or composition for instance are contingent on a number of institutional factors and specific sensitivities which condition the relevance of governance rules directed to them. For example, in the large-shareholder control system specific to most Continental European countries, the agency problem is between minority shareholders and dominant shareholders and the board of directors is often controlled by external directors linked to large shareholders: as such, there is no need for Code's rules on proportion of non executive directors. Consequently, codes' rules relating to Anglo-Saxon business context but intended to solve deficiencies in the functioning of board and other governance practices in Continental European countries need to be adjusted and adapted to the characteristics of these systems. The 'comply or explain' approach and the public consultation can be considered as potential means to account for continental specificities. The 'comply or explain' approach implies that companies are invited to adhere to the codes' provisions (comply), but are allowed to deviate from them when their specificities so justify, subject to providing adequate explanation (explain). This has the advantage to allow companies to draw up their governance according to their individual needs and therefore enables them to reflect sector and enterprise-specific requirements (Wymeersch, 2005). In this respect, codes of corporate governance provide voluntary means, i.e. not legally binding,<sup>12</sup> to improve governance practices. The implicit logic of this approach is that the implementation and enforcement of Codes are left to external forces (market pressure and social class influence). As to the consultation process, it nominally seeks to involve interested parties (business actors) in the drafting of the recommendations, in an attempt to take into account their business context and ensure that they will broadly adopt the governance standards designed for them.

However, the lower enforceability of such norms (Cuervo, 2002) and the reasons leading to the adoption of codes of corporate governance in Continental Europe limit the operativeness of these mechanisms and thus the ability of codes to efficiently address these countries' main governance problems. Following Cuervo's rationale, the type of a country's legal system (common and civil law traditions) will limit the efficiency in the application of governance codes. Since they cannot be legally enforced in civil law countries<sup>13</sup> (Continental European tradition), codes are more likely to be applied formally according to the letter but not to the spirit of the law. Equally, De Jong & al (2005) showed that self-regulations initiatives based on voluntary compliance with no monitoring and no (legal) enforcement of compliance – as it is the case for most codes in Europe except UK – are rather ineffective to enhance corporate boards and governance practices. Actually, due to relatively illiquid capital markets with limited control ability in Continental European countries (Cuervo), it is doubtful whether market-led enforcement is a valid instrument for ensuring compliance with governance codes (Wymeersch, 2005).

The worldwide adoption of (similar) codes also calls the effectiveness of codes into question. Both endogenous forces (efficiency argument) and exogenous pressures (legitimacy argument) trigger the adoption of codes of good governance in a country (Aguilera & Cuervo-Cazurra, 2004). Following the efficiency argument, governance standards are adopted to compensate for deficiencies in legal

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<sup>12</sup> However, the Codes can be coercive when they receive legal backing (as in Germany and the Netherlands) and particularly when they are included in listing rules (UK).

<sup>13</sup> According to these authors, in civil law countries where laws that guide the conduct of companies can only be developed in the parliaments, judges cannot enforce the application of codes with the force of regulations, contrary to common law countries (Anglo-Saxon countries).



system regarding shareholders protection and governance structures. Especially in Continental European countries, where the governance rules regarding listed companies do not genuinely reflect the changing conditions in governance arena, they adequately complement the Company Law, often too rigid and complex. They can mitigate its imperfections regarding the working of corporate bodies and the organization of power in (listed) corporations, matters that have generally been left blank, not detailed or in need of updating in the law (Wymeersch, 2007). According to Aguilera & Cuervo-Cazurra they are the rapid way to fill gaps in legal system by providing a means to tackle the problems of transparency and accountability of board and management practices. Conversely, the legitimacy argument claims that under the globalisation forces, national stock exchanges, domestic associations and governments are driven to conform to international governance practices socially defined as efficient and appropriate. By legitimizing domestic companies in the global financial market, countries increase their attractiveness to foreign investors and secure their access to capital. In this view, the adoption of codes does not necessary entail an improvement but instead fulfil symbolic requirements. Unexpectedly, recent studies (Aguilera & Cuervo-Cazurra, 2004; Zattoni & Cuomo, 2008) showed that the development of codes in Continental European countries is triggered more by legitimacy arguments than by the determination to improve governance practices of national companies. Despite the awareness of the need to enhance the efficiency of national governance systems some forces may slow down their development and limit the changes in national governance. For instance the presence of large controlling shareholders, hallmarks of Continental European system, can prevent the adoption of effective governance practices when they undermine the private benefits of control groups (Zattoni & Cuomo). These authors have found that the prevalence of legitimacy arguments in civil law countries leads to the adoption of codes with more ambiguous and lenient recommendations and with either the same or even narrower coverage than codes developed by common law countries. The legitimacy arguments manifestly explain the Anglo-Saxon orientation that characterises many national codes (Akkermans & al. 2007). Along the same lines, we contend that the mechanisms (mentioned above) used to match governance standards with the existing system may not be effective in Continental European countries. Indeed, whereas deficiencies in a country's governance system are strictly related to its legal tradition, corporate governance codes across countries reflect insufficiently these differences in companies' institutional environments. True some codes contain principles on 'conflict of interests', 'employees' role', related to specific governance problems in Civil law countries. In fact, they reflect the governance issues covered by laws and cover limited aspects of these issues, mainly those regarding conflicts of interest. It appears that recommendations regarding the behaviour, the structure and the functioning of boards, which constitute the core of corporate governance codes, are similar across countries. This lack of contextualisation of governance standards to Continental specificities, mainly those related to boards, calls the ability of codes to promote board effectiveness and address the main governance problems in these countries into question even further.

We will investigate these issues through the empirical analysis of the Belgian Corporate Governance Code (hereunder BCGC or the Code). As elsewhere in Europe, a corporate governance committee ('Lippens Commission') was established, at the initiative of three institutions representative of the business milieu<sup>14</sup> within the Belgian employers association, to draw up a Belgian code of reference for all listed companies, based on 'comply or explain' principle. On June 18, 2004, the committee published its first draft on its website and invited the corporate actors concerned (listed companies) to come up with suggestions<sup>15</sup> for improvement. The comments received, together with recent EU

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<sup>14</sup> The main regulatory body of the financial system (*Commission Bancaire Financière et des Assurances – CBFA*), the Belgian Employers Association (*Fédération des Entreprises de Belgique – FEB*) and financial market authority (Euronext-Brussels).

<sup>15</sup> With more than 300 pages of comments received during the two (summer holidays) months of the consulting phase, the Committee considered that the public consultation held on the draft Code was a success.

Commission initiatives, led to changes to the initial version. The final Code was published on December 9, 2004 and came into force on January 1<sup>st</sup>, 2005<sup>16</sup>. It contains recommendations and suggestions (provisions structured under nine principles and some guidelines) of good and responsible governance reflecting internationally recognized best practice. Only the provisions are subject to the ‘comply or explain’ principle. As part of our assessment of the Belgian’s self-regulatory initiative, we wonder to what extent the public consultation held on the draft code to involve interested parties in the drafting of the final version of the Code has allowed for consideration of Belgian peculiarities; and whether the ‘comply or explain’ approach really allows for contextualization and scalability needed to take account of the specificities of a wide variety of companies. The analysis summarized hereunder is aimed at revealing any ‘acclimatization’ process to the Belgian business context of codes originated in the Anglo-Saxon world and at reflecting the extent of the compliance of Belgian firms with the Code’s recommendations.

**Methodology**

We assess the BCGC’s effectiveness in promoting efficient governance structures by means on content analysis of three documents: the code, its first draft and the comments and suggestions received from the public consultation. The purpose of this analysis is to examine whether Belgian listed firms deem the recommendations laid out in the Code to be appropriate to the local governance practices and whether the governance model favoured by the BCGC deals with the governance problems of most of them. The examination of the suggestions and critics expressed, on the one hand, and the comparative analysis of the draft code and its definitive version on the other hand, enable us to discern to what extent the comments convey some reluctances as to the governance model advocated by the Code and whether the changes made in the draft code take into consideration the requests for greater contextualisation and finally to evidence the success or failure of this Code.

**Table 1 STRUCTURING OF THE BELGIAN CORPORATE GOVERNANCE CODE (BCGC)**

<b>Theme 1</b> : The Governance structure	PRINCIPLE 1. The company shall adopt a clear governance structure PRINCIPLE 6. The company shall define a clear executive management structure
<b>Theme 2</b> : The composition and the functioning of the board, the role, the rights and the duties of directors.	PRINCIPLE 2. The company shall have an effective and efficient board taking decisions in the corporate interest PRINCIPLE 3. All directors shall demonstrate integrity and commitment PRINCIPLE 4. The company shall have a rigorous and transparent procedure for the appointment and evaluation of the board and its members PRINCIPLE 5. The board shall set up specialised committees
<b>Theme 3</b> : The remuneration of directors and executive managers	PRINCIPLE 7. The company shall remunerate directors and executive managers fairly and responsibly
<b>Theme 4</b> : Other issues of the Code	PRINCIPLE 8. The company shall respect the rights of all shareholders and encourage their participation PRINCIPLE 9. The company shall ensure adequate disclosure of its corporate governance

<sup>16</sup> Subsequently, the Committee undertook an updating of the BCG Code to heed changes in legal and business practices as well as international financial markets requirements and regulatory developments. A new version of BCGC (Code 2009) has been published, following a new public consultation. The 2009 Code, which does not seem to bring about dramatic changes, is not the subject of this article.

Data analysis involved various applications of sorting, organizing and coding data. We started organizing the comments received in concordance to both the draft code and the final Code in order to determine the number of comments for each provision and to be able to analyze their importance and relevance. The comments (from 73 organisations and people) were written either in French, English or Dutch. However, only the comments in French and English are the object of our empirical analysis by reason of financial motives (translation costs of Dutch comments). The comments were indeed divided and matched with the different sections of the preamble and the different provisions of the Code<sup>17</sup> they were meant for: we came out with a total of 514 different comments and suggestions to be into consideration in the analysis. Subsequently, we identified and sorted all the modifications introduced in the definitive version<sup>18</sup>. Finally, we also structured the Belgian Code (consisted of 9 principles or “pillars on which good corporate governance should rest” in the Committee’s opinion) according to board issue and the other issues addressed by the Code: four topics were highlighted (see table 1 above). Only the first three themes regarding the board of directors’ issues were analysed in full: the governance structure (principles 1 and 6), the composition and the functioning of the boards as well as the role, the rights and the duties of the directors (principles 2 to 5), the remuneration of directors and executive managers (principle 7). The results displayed below regard however two out of three themes (2 & 3).

## Results

### ***Overall assessment of the Belgian Corporate Governance Code (BCGC)***

In the main, the content analysis suggested that the BCGC exerts formal rather than effective influence on the corporate governance structure and practices of Belgian listed companies. A detailed analysis of both versions of the Code revealed that the BCGC does not differ significantly from the draft Code as regards the content and the conception. The definitive text of the provisions is generally based on the text of the principles and provisions in the draft Code. The main amendments that have been made following the public consultation concerned the form of the Code and some provisions<sup>19</sup>: reframing and withdrawal of many overlapping rules regarding disclosure and transparency, explanations regarding the different sets of rules and the ‘comply or explain’ principle, incorporation of non clear-cut or even ambiguous norms into a new set of rules, the Guidelines (see below).

The analysis of BCGC evidenced that the Committee, as elsewhere in Europe and Anglo-Saxon countries, sought to prod boards into effectively overseeing executive managers and hold both managers and boards accountable to investors. Consequently, the core of the recommendations (themes 1 & 2) seek to strengthen the independence of board members and empower them through the three key governance measures reported earlier. We did find provisions (theme 2) similar to those introduced in the Combined Code following the Higgs Review and related to the process-oriented view of board effectiveness as highlighted by Roberts & al (2005) to create accountability. Many recommendations in this topic focused on the key role of the chairman for the effective functioning of the board; the definition of the role of non-executive directors; the directors’ evaluation process, induction, training and continuing professional development. However, these

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<sup>17</sup> See the Committee’s website [www.corporategovernancecommittee](http://www.corporategovernancecommittee), for the structure and the form of the draft code and the BCGC.

<sup>18</sup> The modifications made in the draft code were classified according the following categories: Addition (A), Withdrawal (R), Substantial Modification or full change of the initial idea stated in the draft (M), Minor Modification that does not change the sentence’s basic idea (M \*) and Displacement (D).

<sup>19</sup> We have found 52 Additions and 88 Withdrawals of sentences or paragraphs, 85 Substantial Modifications or full changes of the initial idea stated in the draft, 69 Minor Modifications and 12 Displacements (D).

recommendations are less stringent, more lenient than those introduced in the Combined Code, especially in the last version. Given the reluctance showed by interested parties regarding the evaluation process, the nomination and the induction of directors – relatively new rules in the Belgian business context where controlling shareholders have a key influence on the board’s members appointment and companies management – the Committee considered in the final version many of these provisions as mere guidelines and deleted the others. Guidelines are to help companies to interpret the provisions laid down in the code and are mainly qualitative; they do not lend themselves to assessment in terms of compliance. Obviously, these guidelines and other lenient recommendations were not considered in different quantitative studies claiming the success of BCGC.

The Code also highlighted transparency and disclosure<sup>20</sup> standards (Themes 3 & 4) with respect to financial and non-financial information, in emulation of the rules existing in market oriented systems. In this respect, it turns out that disclosure of detailed information regarding board members and executive managers, in particular of their remunerations as advocated by the Committee, is quite unusual within Continental European countries (Belgium included). While the code paid some limited attention to the shareholders (Theme 4), it did not really address the main governance problems of most Belgian listed company: the agency problem between minority shareholders and dominant or even controlling shareholders and the conflicts of interests arising from ownership control. Indeed, the Committee disregarded the request made by companies during the public consultation to integrate the rights and duties of dominant shareholders in the board’s structure and functioning and thus avoided tackling the issues raised by the presence of dominant shareholders in many boards of directors. It comes out this set of elements that the Committee tried to enhance investors’ confidence as to the adequacy of board governance (perceived effectiveness) rather than promote efficiency of governance practices in these companies, or even actual board effectiveness in the sense we have defined above.

This analysis substantiated the Anglo-Saxon orientation of BCGC and in general the converging trend in organisational practices worldwide (Aguilera & Curevo-Cazurra, 2004). The idea of commending governance structures modelled on the Anglo-Saxon business context, quite different of Continental Europe’s one, reflects actually the implicit aim of the Belgian governance reform. What it is about is first and foremost opening up the companies to international financial markets and enabling them to meet the expectations as regards the standards of behaviour and accountability of board and rules of transparency in financial and non financial reporting. In a globalisation context, it appeared indispensable to increase transparency of national capital markets in order to make them less illiquid and improve market control mechanisms. Such an approach is consistent with a symbolic perspective on corporate governance or legitimizing logic advanced by some scholars to explain the worldwide diffusion of the (similar) codes. The prevalence of legitimacy arguments entails that rules underscoring the importance of board behaviour and relationships are introduced regardless of the extent of their implementation. This prevalence also limits the BCGC’s ability to significantly address deficiencies in the Belgian corporate governance system and enhance efficiency of board functioning within listed companies. Since the Committee adopted a conception of governance focused on the agency conflicts, the governance reform in Belgium did not really provide companies with the appropriate model to solve deficiencies in their governance structure. The analysis of comments undeniably illustrated this lack of contextualisation. Contrary to the Anglo-Saxon context where the board has to control management, in Belgium the board has in the main to minimise the power of the controlling shareholders over the management and protect weak minority shareholders

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<sup>20</sup> According to the Committee, “disclosure is crucial to allow for an effective functioning of outside monitoring. Hence the Code’s provisions aim at putting in place a high level of transparency concerning companies’ corporate governance”.

(Dehaene & al, 2001). Accordingly, as the analysis of the comments indicated that the critical provisions which did not fit with the existing practices are those related to the composition of the board and its committees, the independence of some non-executive directors and of the board itself, as well as the disclosure of remuneration policy. Next, we turn to these critical recommendations that receive less agreement among Belgian listed firms and other suggestions disregarded by the Committee (themes 2 & 3). In this respect, follow-up studies undertaken by the Federation of Belgian Enterprises (FEB-VBO), the Belgian Governance Institute and private firms (KPMG Advisory & CORGO, 2006; Claeys & Engels, Law firm, 2006) come to strengthen our results.

### ***The composition and the functioning of the board and the role and the duties of directors***

The provisions that come under this heading deal with the adequate composition and the independence of the board, making possible efficient decision-making and internal functioning of the board (principles 2, 3, 4 & 5). In this respect, the analysis revealed that BCCG went beyond (recent) legal requirements on corporate governance issues and introduced bold initiatives, especially regarding the composition of the board, the mandatory appointment of audit, remuneration and nomination committees and their composition (Bogaert & Peeters, 2003, Agboton, 2007). Other similar initiatives include the mandatory appointment of a secretary to the board – a position unknown in Belgian Company Law, the setting up of rigorous appointment and evaluation procedures and an induction programme for board members, the criteria of independence that some directors must meet and the specification of the role of the chairman, both as leader and facilitator (Agboton; Van Der Elst, 2008). These board-related measures are precisely what came under fire from many commentators for the reason that they did not match with common practices in Belgian listed companies, and more particularly with the Belgian corporate governance model. Indeed, while the Committee asserted in the preamble that “Belgian listed companies are often controlled by one or more major shareholders” (final version) and “different shareholding structures entail different potential conflicts of interest or agency conflicts for which specific governance recommendations will be necessary” (draft only), neither version of the Belgian Code (draft and BCGC) addressed these specific Belgian features – except provisions 4.6 (see below) and 8.12. As evidenced by the literature, the presence and the influence of large shareholders (often ‘holding companies’) in most listed (and many unlisted) firms are a core issue for Belgian corporate governance. Due to the major role some of them played in economic and industrial development of Belgium during the 19<sup>th</sup> and early 20<sup>th</sup> centuries, large shareholders acquired and still have a lot of influence over companies in which they invest (Wymeersch, 1994). It not unusual for these shareholders to play an effective monitoring function, to give management, financial and technical assistance, take the helm of board and fix the corporate strategy through their presence or the presence of their representatives (non-executive directors) in board and management committee: they are willing and able to wield power over companies. In this respect, this type of ownership and control makes it possible to deal with the agency problem between shareholders and managers and the free riding problem in large organizations (Shleifer & Vishny, 1986). Given the weight of reference and control shareholders in Belgian listed companies, it is striking that none (or very few) of the provisions related to board structure (2), composition of the committees (5), selection and assessment of directors (4) is making reference to them. It came therefore as no surprise that the commentators called for integration of the rights and duties of large shareholders in order to reflect the economic reality of Belgian corporations.

With regard to board composition, the principles enunciated in the draft required a balance between executive directors, independent non-executive directors and other non executives and that “no individual or group of directors should dominate the board's decision-making”. Commentators considered them to be inappropriate for Belgian listed firms under control as they



appear as preventing controlling shareholders from exercising their rights; it is deemed that even the existence of the non-compliance option would not make these rules acceptable. Furthermore according to one of them *“that is the responsibility of the shareholders to decide on the definition of “balanced composition” taking into consideration the specific needs of the company... A majority of board members representing a reference shareholder does not per se constitute a dominant position, neither does the fact that a number of directors would vote in a same manner, but in full respect for their responsibility as a director”*. The Committee did not make any modification to these rules and added that “no individual should have unfettered powers of decision-making” (first part of provision 2.2 in BCGC). Moreover there is no requirement for companies to include these points in the “Corporate governance Charter” and the “Corporate governance Chapter” of the annual report, two documents intended to ensure disclosure of sound corporate governance practices. Due to the qualitative nature of these provisions (non verifiable based on publicly available information) they were not analysed in the follow-up studies of BCGC. In order to assess the ability of the board to operate efficiently, follow-up studies then restricted themselves to considering the sole objective information as regards board composition and independence. Though, composition rules provided for by BCGC do cause some concerns.

Actually, the existence of core shareholders in Belgian listed companies – as elsewhere in European countries – is giving rise to a specific governance problem that these recommendations are unable to deal with adequately, namely the conflict of interests between controlling shareholders and minority shareholders. Using the competence they have to determine corporate strategy and appoint the (majority of) board members, controlling shareholders can and do give priority to their own interest at the expense of the interest of the company they invested in and of its minority shareholders, for instance by shifting corporate resources away from the dominated company or restricting its activities. They set the tune even in listed corporations. This explains the characteristic of boards’ composition within Belgian listed corporations: they are often dominated by non-executive (outside) directors, representative of controlling shareholders (Dehaene & al, 2001; Van Der Elst, 2008). From this viewpoint scholars admitted that corporate reform in Belgium must seek to reduce the influence of these shareholders over the board in order to ensure that decisions are made in the corporate interest and to favour management’s independence instead of curtailing its powers. In particular, as regards the board composition, there is a need to reduce the number of directors (non executive directors) representative of large shareholders. We noticed nevertheless that the second part of provision 2.2 regarding board’s composition is even less likely to counter the traditional powers of majority shareholders and then help companies to address deficiencies in their board structure or increase transparency in their management and governance. The Committee recommends that “at least half the board should comprise non-executive directors ...”. Such a proposition does not indeed bring any real change to board’s composition of Belgian companies insofar as it keeps the possibility open for companies to have a majority of non-executive directors. Moreover the definition of a non-executive director provided in the associate guideline – “A non-executive director is any member of the board who has no executive responsibilities in the company” – does not exclude large shareholders representatives. Therefore, it is hardly surprising that follow-up studies of BCGC showed that most companies comply with this recommendation. If this recommendation actually conformed to the Anglo-Saxon standard regarding board composition, it does not prevent some board configurations leading to conflicts of interests and deadlock situations within family-controlled and holding companies. These findings suggest that even if the BCGC rules, especially those related to board structure, contain no reference to large shareholders, the committee, in drawing up the code, was indeed influenced by their existence and positioning in the Belgian corporate sector. As a result, the BCGC, while conforming to internationally recognised standards, failed to bring significant changes in and improvements to board composition and functioning. As this analysis illustrated, the focus on board composition and other structural governance information may provide misleading information as to the functioning of the board. The Belgian case makes it clear that the mere



adoption of recommended structures and practices is not the ultimate solution to ensure sound corporate governance.

One of the radical suggestions in the draft referred to the composition of audit committee: it required that all the members of this committee be independent non-executive directors. Once again it is a full transposition of the Anglo-Saxon recommendation. This provision was manifestly inappropriate for the Belgian business context where large shareholders have a say in this matter like in other ones regarding the management of corporations. Significant criticism from commentators has led to its amendment: the new provision requires that the committee be composed exclusively of non-executive directors and at least a majority of its members should be independent. Implicitly, it suggests that companies can introduce at least one representative of large shareholders. Despite this change, follow-up studies showed that only a small majority of the BEL-20 (the 20 biggest listed firms) companies comply (or give reason for non compliance) with this provision and that the extent of compliance is lower for medium and small listed firms where the establishment of audit committee is less frequent. As to the composition of remuneration and nomination committees (majority of independent non-executive directors alike), most firms provided explanations for non-compliance with these provisions. Actually, the analysis of comments showed that some firms doubt that the composition called for by the BCGC for committees will improve efficiency of their boards regarding mainly remuneration and nomination issues and then do not see the necessity to change their board structure. It might well suggest that the rules regarding sub-committees composition still do not fit with common practices. In this respect, the Swedish case may be instructive for regulators willing to ensure a formal and objective nomination process in companies with large shareholders. Indeed, one can find in Swedish companies what they call 'external committees' composed of large shareholders, including institutional investors and chaired by the chairman, who coordinates and provides transparency to the appointment/nomination process (OCDE, 2004). According to the follow-up studies, one third of all companies do not form any subcommittee and two-thirds combine nomination and remuneration committees. Non compliance with these provisions occurs mainly in smaller companies and to a lesser extent in medium companies: roughly 50% do not have a nomination committee. Similar findings in other countries led some scholars to conclude that smaller listed companies do not need committees for improving efficiency of their board, suggesting that it may be relevant to have different kinds of rules for small and big companies.

Provisions regarding the selection and assessment procedures are equally bold initiatives. To improve the quality of board and reduce the informality surrounding the appointment and nomination of directors, the committee, in line with the Higgs Report, has put a lot of emphasis on clarity, objectivity and transparency of the entire process of appointment or re-election of board members. Some commentators asserted that the nomination model advocated by the BCGC is unsuitable for Belgian listed firms since it is specifically suited to the case of companies where ownership is fully dispersed. It must be kept in mind that, in Belgian companies, controlling shareholders exercise a decisive influence on the appointment of the majority of directors. Yet, as pointed out in the comments, nomination of directors is in Belgium like in most if not all Continental Europe countries a genuine shareholder prerogative exercised by the General Meeting. The most 'extremist' comments seem to consider that it cannot be shared with any other corporate organ. If some of the commentators admitted that pre-established rules or profiles may apply to all candidates (those proposed by large shareholders as well) in order to improve the nomination process, they considered that the requirements formulated in the draft were excessively restrictive and imposing unacceptable limits to shareholder discretion in selecting suitable board members.

In reaction to this various comments, the words "to be proposed for nomination or re-election to the general meeting of shareholders" (provision 4.2 in the final version) have been added to the draft's statement that "the board, lead by its chairman and advised by a nomination committee consisting

of a majority of independent non-executive directors, is entrusted with the selection of the appropriate persons". There has been no explicit mention of proposals stemming from controlling shareholders and no explicit reference to the power of (large) shareholders to elect board members. The Committee just came up with a slight change in one of the provisions (§5 of 4.6) to involve – somewhat ambiguously – the nomination committee when the proposal for appointment comes from a shareholder (without any specification with respect to controlling shareholders)<sup>21</sup>. Besides, following the request of some institutions representative of investors (Deminor, ISS, Hermes Pension Management), it also recommended the limitation to a maximum of five of the number of mandates a director may hold in different companies and to a maximum of four years (in contrast with the legal maximum of six years) the duration of directors mandate. We notice that follow-up studies provided no information on these provisions related to the operation of the board, because of their qualitative nature. Indeed, while the Committee invited companies to have a rigorous and transparent appointment procedure, it did not compel them to supply information on this election policy in the corporate governance Charter or Chapter, which leaves too large a leeway for companies to comply only formally. The same happened for provisions regarding the role of the chairman, the induction and professional developments of directors and the assessment of boards and its members recommended by the draft to reinforce the effectiveness of the board. They explicitly refer to the behaviour and internal relationships of board members, the chairman's interaction and communication with non-executive directors and the CEO, provisions that according to McNulty & al (2005) can promote positive board dynamics. According to the critics<sup>22</sup> however, we can notice that in the BCGC a lot of such rules (non executive roles, evaluation of the board of directors) are now mere guidelines and then less stringent: they are of qualitative nature and cannot be evaluated by means of publicly available data. Likewise, no information must be disclosed in the corporate governance Charter or Chapter regarding the evaluation procedure of directors' activity. Moreover the requirement of an annual individual evaluation and the rule submitting to rigorous review a non-executive director's mandate of a total duration above 12 years have been abandoned. While the provision requesting the organisation of meetings between non-executive directors in the absence of the CEO or the executive directors was maintained, companies seemed to misunderstand its significance for an effective contribution of board members: the follow-up studies evidenced a weak compliance with this provision (30% of companies mentioned it). In the main compliance with provisions regarding operational activities of board is low<sup>23</sup>. The fact that the codes contain many qualitative or lenient recommendations which are practically difficult to assess increases the possibility of formal rather than substantive compliance (Werder & al, 2005; Akkerman & al. 2007).

The influence of large shareholders in the drawing up of the code may also explain the presence in the draft of lenient and vague provisions regarding the independence of directors. As noticed mainly by shareholders representative institutions, the draft code provided no definition of this key concept and contained a mere reference to article 524 of Company Law as regards the criteria of independence a board should apply. Yet, the rules of independence set out in Belgian Law are only suitable to the specific situation of intra-group conflicts of interests. According to the comments of shareholders representatives, the provisions in the governance code *"should refer to best Corporate Governance practice, rather than minimum practice given the fact that the definition and the role of independent directors are of paramount importance to insure appropriate checks and balances within the board"*

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<sup>21</sup> For other alternative, enabling to take effectively major shareholders into account in the nomination process, see Sweden case mentioned above.

<sup>22</sup> Deminor stated that *"this is in line with investors' expectations and with the most recent codes' provisions. It is however a big step for boards and it will require a change in mentality. The danger might be to do too much, too fast and to transform this exercise in an automatic box ticking"*.

<sup>23</sup> Annual reports provided hardly any information on self-assessment of the board; only a small majority of listed companies (large to small) disclosed director's participation to board meetings; 30% of the companies explicitly reject the limitation at five of directorships in listed companies.

*of directors and that independence is of vital importance for the process of supervision*". The BCGC contains now a proper definition of independence (2.3) and refers to the criteria of independence laid down in the European Commission's Recommendation 'on the role of non-executive or supervisory directors' (appendix A). For some commentators however, what is at stake with this issue is to realize that independence per se is not the panacea for inadequate monitoring or conflicts of interests problems occurring within the board. The point of how to measure effectively the independence of a director and make the concept operational remains questionable. As evidenced by the case of Enron, exhibit compliance with criteria of independence is not a sufficient guarantee of effective independence; independence (of mind) is merely one of the attitudes a director may adopt in order to contribute efficiently to decision-making processes and other board activities. In this respect, some commentators called for a greater emphasis on the involvement, competence and responsibility of directors, when defining their role and duties. Unexpectedly, the attempt of the Committee to define the task of non-executive directors similarly to the Higgs Report, i.e. in a way that can create accountability (in the above defined meaning) within the board, appeared misunderstood. Many commentators considered that such a definition is at odds with the principle of collegial decision making, which is a central feature (of jurisprudential origin<sup>24</sup>) in the functioning of Belgian boards. As a result, some of these provisions are now mere guidelines of BCGC's provision 3.3 stating that "while executive and non-executive directors are part of the same collegial body, they have each a specific and complementary role to play on the board", while other ones have been deleted. As to the criteria adopted for director independence, the follow-up studies showed that companies opted for many different definitions, making it difficult to have an objective assessment of this provision: some referred to legal standards, others used the BCGC's rules, a small majority applied a combination of both standards and a limited number of companies referred to other standards. Among the 40% of companies which disclosed a list of criteria applied, at least half of them diverged from BCGC criteria.

In sum, whereas the committee appeared aware of the dominance of controlling shareholders in most listed (and unlisted) companies, none of the BCGC's provisions related to board structure and board composition took explicitly this Belgian peculiarity into account, as required by commentators. Some of the latter even suggested to distinguish within the Code controlled companies from diversified companies in order to provide appropriate rules for each. The stance of the Committee therefore made it difficult to address some major deficiencies in the Belgian corporate governance model, especially those related to board functioning. The adaptation of international standards to the economic reality of Belgian companies appeared very limited and many recommendations in the BCGC (provisions and guidelines) have low stringency – some are even merely qualitative – and thus prevent any appropriate assessment of board effectiveness or code compliance. Actually, the market-driven approach of the Belgian corporate governance reform (Van Der Elst, 2007)<sup>25</sup> explains this lack of contextualisation. The chief objective was to increase the competitiveness of Belgian companies, enable them to operate on a larger market and broaden their shareholding base by inviting them to comply as closely as possible with international standards of corporate governance in order to meet international capital market requirements of greater disclosure and transparency (legitimacy arguments).

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<sup>24</sup> It is deduced from one provision of art. 522 of the Company Law which stipulates that "...division of labour among directors cannot be opposed to third parties, even if publicized in the legal forms...".

<sup>25</sup> According to this author, as Belgium had not experienced major corporate collapse, the absence of a Belgian Code is felt to be damaging to the position of the Belgian capital market and Belgian listed companies. This also explains the introduction of some corporate governance issue into Belgian corporate law (Law of 2 august 2002) and the relatively late adoption of corporate governance standards.

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### ***The remuneration of directors and executive managers***

An area of particular concern in the corporate governance debate is the compensation of directors. Being aware that, in the wake of recent scandals, the market was demanding for more disclosure on this point, the Committee clearly went beyond legal requirements and common practices and produced very detailed rules regarding the remuneration policy as well as the disclosure of directors' (individual) remuneration packages. For instance it advised against granting performance-related remuneration such as attribution in a way or another of company's shares, profit sharing and attendance fee, this latter practice being explicitly provided by the law and widespread within companies. Pursuant to agency theory, the idea behind the disclosure of such items is that this information is crucial for shareholders (external investors) to judge the competence and independence of board members as well as the costs and benefits of remuneration plans and the contribution of incentive structures (OCDE, 2004) to performance. In this respect, details about the structure of the compensation scheme are as important as the overall level. According to Peeters & Bogaert (2003) the full disclosure of direct and indirect remuneration of each individual member of the board or of the management committee, including pension schemes, termination benefits and golden parachutes is obviously revolutionary with respect to Belgian standards. Indeed, in continental European countries, contrary to Anglo-Saxon countries where remunerations have been published for a long time on an individual basis, they are disclosed anonymously and on an aggregate basis for the entire board and management. Despite the call of most commentators for a limitation of the scope of these provisions, the Committee decided to maintain its original recommendations, subject to the addition of some provisions for the establishment and disclosure of a remuneration policy – in particular for the executive managers. As a result, compliance with many of the provisions pertaining to this principle was weak, particularly for small companies. It appeared that the annual report provided incomplete information on board remuneration and did not offer the required transparency: only 60% disclosed the remuneration package of the CEO, of which only 27% explained the lack of disclosure; the globalised compensation packages for other management members (published by 94% of companies) were not comparable due among others to the huge differences in the number of executive managers; only a small majority of companies disclosed information on the main contractual terms of hiring and termination arrangements with executive managers, the different elements of the remuneration package (fixed, performance-related and long-term incentive components) or the number and key features of shares, share options or any other right to acquire shares, granted on an individual basis during the year to the CEO and the other executive managers.

### **Conclusion**

Our research investigated the role of codes of corporate governance as a way to improve the effectiveness of board in Continental European countries. First, evidence from our analysis of the Belgian corporate governance code confirmed that governance reform based on codes is more likely to improve perceived effectiveness rather than actual effectiveness, due in part to the rationale behind the adoption of such codes and in part to the difficult access to information about the actual functioning of the board. Given the positioning of dominant shareholders and holding companies in Belgian listed companies, one would have expected that the Code would pay some attention to them and address the governance issues they are raising. On the contrary, it appeared that the Belgian regulatory bodies sought to promote international standards by increasing transparency in decision-making organs through three central items (separation of the functions of chairman and CEO, composition and independence of the board, creation of board committees), chiefly with the view to enhancing their competitiveness on the capital markets. This legitimacy motive explained why the Code elaboration process (given the systematic neglect of some criticisms and suggestions issued during the consultation phase) did not allow for consideration of the business context of Belgian listed companies. Moreover, even if the 'comply or explain' principle can allow for such consideration

of specific business features, our analysis reveals that it is in most cases ineffective as it leaves too much room for symbolic rather than actual compliance. We clearly pointed out that recommended best practices regarding board functioning and structure did not match with common practices and above all appeared inappropriate to help companies to remedy the deficiencies in their board. Furthermore the attempt of the Committee to provide beside the traditional rules some process-oriented provisions did not yield significant outcomes as to the actual board effectiveness: the explanation is that most of them are merely qualitative. Not only qualitative information on the activities of the board and its subcommittees remained scarce in corporate governance Charters and Chapters but, more fundamentally, such activities do not lend themselves to external assessment, as some follow-up studies evidenced.

Contrary to the quantitative empirical studies claiming the success of the Belgian Code, our findings suggested that this initiative has had little impact as a means to remedy deficiencies in corporate governance practices. True, the follow-up studies showed that the Code actually has contributed to increase the awareness of the importance of sound governance among Belgian companies and shape some changes in Belgian boards. As noticed by Wymeersch (2007), such studies however are unable to verify the substance of the disclosure and the extent to which the companies have effectively adhered to the rules: they are restricted to formal assessment. In this respect, our findings support the idea that outward compliance with corporate governance standards is not a sufficient guarantee of their effective operation. Thus, to assess both codes and board effectiveness, there is a need for future research to move beyond the structural aspects of corporate governance and focus on the substantive information regarding the board activities. From a policy perspective, there is also a need to base governance reform on an informed understanding of the actual determinants of board effectiveness, in a sense that could reinforce the ability of codes to deal effectively with the balance of powers inside of the corporation.

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