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Cultural Difference and
Corporate Governance

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Cultural Difference and Corporate Governance

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I. GEERT HOFSTEDE AND THE MEASUREMENT OF CULTURAL DIFFERENCE	190
II. HOFSTEDE AND COMPARATIVE CORPORATE GOVERNANCE.....	193
III. CRITIQUE OF BUCK & SHAHRIM'S MODEL.....	199
IV. A REVISED MODEL	200
V. POLICY IMPLICATIONS: CONVERGENCE AND DEVELOPING ECONOMIES	206
VI. CONCLUSION: LOOKING AHEAD.....	209

The unmet challenge of the corporate governance literature remains better to conceptualize the firm and its governance structures in terms of their *embeddedness in social structures*.
— Gregory Jackson¹

Corporate governance worldwide exhibits remarkable diversity. Public corporations in the United States feature diffused shareholder bases that supervise and motivate management through strong boards, incentive-based compensation, rigorous disclosure requirements, and an active market for control. Japanese firms on the other hand use cross-shareholdings, credit facilities, and interlocking boards to organize themselves into *keiretsu* groups, an arrangement that entrenches managers and subjects them to the discipline largely of their peers.² In Germany, management of a public

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¹ Gregory Jackson, *Comparative Corporate Governance: Sociological Perspectives*, in *THE POLITICAL ECONOMY OF THE COMPANY* 265, 267 (G. Kelly et al. eds., 2000) (emphasis in original).

² See generally MARK J. ROE, *STRONG MANAGERS, WEAK OWNERS: THE POLITICAL ROOTS OF AMERICAN CORPORATE FINANCE* 177–82 (1994). On the evolution of *keiretsu*, see Randall Morck & Masao Nakamura, *Been There, Done That: The History of Corporate Ownership in Japan* 77–79 (European Corp. Governance Inst. Working Paper No. 20, 2003), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=422120. But for a critical, contrary view which argues that the *keiretsu* constitute nothing more than a legend inspired by Marxist economists in Western universities, see Yoshiro Miwa & J. Mark Ramseyer, *The Multiple Roles of Banks? Convenient Tales from Modern Japan*, in *CORPORATE GOVERNANCE IN CONTEXT: CORPORATIONS, STATES AND MARKETS IN EUROPE, JAPAN AND THE U.S.* 527, 563 (Klaus J. Hopt et al. eds., 2005).

corporation answers largely to its employees, who exercise control through codetermination vehicles, as well as to banks, who exercise influence through creditor mechanisms and the *Vollmachtstimmrecht* (the power to vote their brokerage clients' shares).³ In France, the state has historically taken an active role in the economy, fostering "national champions" and influencing public companies through subsidies and "golden shares."⁴ In many other countries, individuals, families, institutions—or coalitions of these forces—control corporations through various arrangements that include large block holdings, multiple share classes, cross-holdings, pyramids, circular structures, corporate charter provisions, and non-voting depository receipts.⁵ The categories of dominant shareholders vary from country to country and can include industrial or financial holding companies (Belgium),⁶ cooperatives (Denmark),⁷ the state (Austria),⁸ mutual funds (Czech Republic),⁹ and leading families (Hong Kong).¹⁰ Secondary shareholders, such as pension funds in Chile, can also play a major role in supervising controlling shareholders if sufficiently motivated and empowered by the country's regulatory regime.¹¹ Each form of corporate governance contains its own set of benefits and costs, and empirical research has failed to demonstrate the incontrovertible superiority of any one system over the others.¹²

³ On codetermination, see MARK J. ROE, *POLITICAL DETERMINANTS OF CORPORATE GOVERNANCE: POLITICAL CONTEXT, CORPORATE IMPACT* 71, 72 (2003). On *Vollmachtstimmrecht*, see W. Carl Kester, *Covernance, Contracting, and Investment Horizons: A Look at Japan and Germany*, in *STUDIES IN INTERNATIONAL CORPORATE GOVERNANCE—COMPARISON OF THE U.S., JAPAN, AND EUROPE* 227, 236 (Donald H. Crew ed., 1997).

⁴ See generally T.C. Melewar & Andrea Mott, *Is the French Model of Capitalism Becoming More Like the Anglo-Saxon Model*, 28(4) *J. GEN. MGMT.* 47, 48 (2003). See also Jeremy Grant & Thomas Kirchmaier, *Corporate Ownership Structure and Performance in Europe*, (Soc. Sci. Research Network, CEP Discussion Paper No. 0631, 2005), available at <http://ssrn.com/abstract=616201>.

⁵ See, e.g., Grant & Kirchmaier, *supra* note 4, at 5–10, 20.

⁶ See Eddy Wymeersch, *Holding Companies in Belgium*, in *COMPARATIVE CORPORATE GOVERNANCE: ESSAYS AND MATERIALS* 67 (Klaus J. Hopt & Eddy Wymeersch eds., 1997).

⁷ Steen Thomsen, *Corporate Ownership by Industrial Foundations*, 7 *EUR. J. L. AND ECON.* 117 (1999).

⁸ Rafael La Porta et al., *Corporate Ownership Around the World*, 54 *J. FIN.* 471, 492–95 (1999) [hereinafter La Porta et al., *Corporate Ownership*].

⁹ Jan Hanousek & Evžen Kočenda, *The Impact of Czech Mass Privitisation on Corporate Governance*, 30 *J. ECON. STUD.* 278, 287 (2003).

¹⁰ Stijn Claessens et al., *The Separation of Ownership and Control in East Asian Corporations*, 58 *J. FIN. ECON.* 81, 83 (2000).

¹¹ Grant & Kirchmaier, *supra* note 4, at 21. On Chile, see Manuel R. Agosin & Ernesto Pastén H., *Corporate Governance in Chile* (Cent. Bank of Chile, Working Paper No. 209, 2003), available at <http://cegopp.cema.edu.ar/download/CorporateGovernanceChile.pdf>.

¹² RADISLAV SEMENOV, *TILBURG UNIVERSITY CENTRE FOR ECONOMIC RESEARCH, CROSS-COUNTRY DIFFERENCES IN ECONOMIC GOVERNANCE: CULTURE AS A MAJOR EXPLANATORY FACTOR* 48–65 (2000).

Scholars and other pundits have offered various explanations for the international diversity of corporate governance systems. Legal explanations focus largely on the differences in regulation suggesting for example, that a country with more mandatory disclosure and rights for minority shareholders has a greater likelihood of developing diffuse shareholding patterns.¹³ Others extend the inquiry beyond corporate law to a broad array of socio-economic factors, including the timing of industrialization, industrial structure, labor relations, pension systems, national population, and wealth.¹⁴ A country with large national banks like Germany, for example, has more potential to develop bank-oriented corporate governance than a country with a diffused banking industry like the United States.

The insufficiency of these models has given rise to efforts, largely pioneered by Mark J. Roe,¹⁵ to explain corporate diversity as a product of differences in national culture. Each culture contains its own set of value-preferences—including such values as family, prestige, public service, wealth, quality of life, patriotism, competition, and generosity. These value-preferences guide the day-to-day decision-making of a firm's investors, managers, employees, regulators, and other stakeholders. The aggregation of these choices can result in an optimal corporate structure and financial system specific to a particular society.¹⁶ Once developed, a culture's corporate regime reinforces the educational, legal, and other institutional factors that give rise to its existence, creating a self-reinforcing cycle.¹⁷ Even if the corporate regime ultimately proves less than optimal, the total costs required to change it may exceed the potential benefits of doing so.¹⁸

However, cross-cultural studies of comparative corporate governance have only scratched the surface thus far. Much of the research to date has been criticized for vagueness, being excessively based on anecdotal evidence, lacking sufficient theory, or else focusing so intensively on certain countries as to preclude application elsewhere.¹⁹ Due to methodological problems inherent in describing culture, broader comparative studies of corporate

¹³ *Id.* at 74–86.

¹⁴ *Id.* at 87–102.

¹⁵ See ROE, *supra* note 2.

¹⁶ It is also possible that multiple equilibriums exist, one with a high degree of investor protection and one without, and two countries may settle for different equilibriums. Eelke de Jong & Radislav Semenov, *Cultural Determinants of Financial Behaviour*, in *INDIVIDUAL IDENTITIES AND THE FINANCIAL MIND* § 1 (Peter Mooslechner & Elisabeth Springler eds., forthcoming) [hereinafter De Jong & Semenov, *CDFB*].

¹⁷ *Id.* § 2.1.

¹⁸ This is known as the principle of path dependence. See generally Mark J. Roe, *Path Dependence, Political Options, and Governance Systems*, in *COMPARATIVE CORPORATE GOVERNANCE*, *supra* note 6, at 165.

¹⁹ Eelke de Jong & Radislav Semenov, *Cultural Determinants of Ownership Concentration Across Countries*, 2 *INT'L J. BUS. GOVERNANCE & ETHICS* 145, 146 (2006) [hereinafter De Jong & Semenov, *CDOC*]. See also De Jong & Semenov, *CDFB*, *supra* note 16, § 2.2.

governance have tended to ignore culture altogether, abstracting it as an unobservable "black box" phenomenon.²⁰ This paper aims to fill this theoretical gap by using a framework developed by management scholar Geert Hofstede.

After introducing the Hofstede methodology for characterizing cultural differences (Part I), and presenting an overview of the research conducted to date (Part II), this paper critiques (Part III) and revises (Part IV) a recent hypothesis that a culture's degree of risk-aversion and collectivism can predict the culture's corporate governance regime.²¹ Application of the revised hypothesis to a number of emerging economies (Part V)—South Africa, Malaysia, Chile, and Hungary—offers insight into how their equity markets might develop and what forms of regulatory reform would prove most useful.

The fact that a country's optimal corporate structure can vary according to its culture has broad policy and philosophical implications. It suggests that the global harmonization of financial regulation comes with costs, and that a limited form of regulatory diversity may prove more efficient than total convergence. The relationship between corporate governance and culture also calls into question the very purpose of a corporation, affording more scope for alternative notions of the firm grounded in stakeholder and team production theory.

I. GEERT HOFSTED E AND THE MEASUREMENT OF CULTURAL DIFFERENCE

Geert Hofstede's seminal study published in 1980 provided the most influential framework for the classification and comparison of cultures.²² The Hofstede study surveyed 116,000 IBM employees in seventy-two countries and extracted from their answers four independent dimensions of cross-cultural difference: uncertainty avoidance, individualism, power distance, and masculinity.²³

Uncertainty avoidance (UA) measures a culture's comfort with unpredictable events. Higher values suggest a more conformist, risk-averse, and generally inflexible society, while lower values suggest a greater tolerance for risk, change, diversity, and ambiguity.²⁴ Japan, Belgium, and

²⁰ Amir N. Licht, *The Mother of all Path Dependencies: Towards a Cross-Cultural Theory of Corporate Governance Systems*, 26 DEL. J. CORP. L. 147, 152 (2001).

²¹ Trevor Buck & Azura Shahrim, *The Translation of Corporate Governance Changes Across National Cultures: The Case of Germany*, 36 J. INT'L BUS. STUD. 42, 44 (2005).

²² GEERT HOFSTED E, *CULTURE'S CONSEQUENCES: INTERNATIONAL DIFFERENCES IN WORK-RELATED VALUES* (2d ed. 2001).

²³ *Id.* at 41. Summaries of Hofstede's framework are found in SEMENOV, *supra* note 12, at 17–23; De Jong & Semonov, *CDFB*, *supra* note 16, § 4; De Jong & Semonov, *CDOC* *supra* note 19, at 149; Licht, *supra* note 20, § III.C.

²⁴ HOFSTED E, *supra* note 22, at 159–61.

Greece all feature high levels of uncertainty avoidance while Singapore, Sweden, and the United Kingdom have relatively low levels.²⁵

Individualism-collectivism (IDV) measures how much people identify with and act through the various groups to which they adhere.²⁶ In more collectivist societies, people establish strong interdependent relationships with their extended families, colleagues, church, and other collectivities that provide protection in exchange for loyalty.²⁷ Such highly collectivist societies include Taiwan, Korea, and Chile.²⁸ More individualistic societies, like the United States and Australia, on the other hand, have higher expectations for people to fend for themselves.²⁹ Power distance (PD) measures how much legitimacy a culture affords unequal distributions of power, wealth, and prestige.³⁰ Societies with greater power distance, such as China, Latin America, and the Arab world, show a greater acceptance of hierarchical structures and status differentials.³¹ Those with lower power distance, such as Austria, Israel, and Denmark, display greater social mobility and more egalitarian norms.³²

Masculinity-femininity (MAS), the most complex and controversial dimension,³³ measures how much a society values assertiveness, competitiveness, status, material acquisition, and other values associated with “maleness.”³⁴ More “feminine” societies, in contrast, privilege harmony, modesty, caring, and quality of life.³⁵ Hofstede cautions against confusing “femininity” with “collectivism.” Individuals can pursue feminine values of harmony and caring, while groups may pursue more masculine endeavors.³⁶ The most masculine countries include Japan, Austria, and Venezuela; the

²⁵ *Id.* at 151.

²⁶ *Id.* at 209–10.

²⁷ *Id.* at 225.

²⁸ *Id.* at 215.

²⁹ HOFSTEDE, *supra* note 22, at 215, 225.

³⁰ *Id.* at 79.

³¹ *Id.* at 87, 97.

³² *Id.*

³³ Hofstede’s use of the terms “masculine” and “feminine” to characterize cultures will strike many modern readers as anachronistic and offensive due to its reinforcement of gender stereotypes. However, because of Hofstede’s prominence, they have become terms of art in management literature on cultural difference. To avoid confusion, this paper uses the established terminology; however, it does not endorse this terminology and would welcome a debate over adopting a new term.

³⁴ HOFSTEDE, *supra* note 22, at 280.

³⁵ *Id.*

³⁶ *Id.* at 293.

most feminine countries include the Scandinavian countries, Costa Rica, and the Netherlands.³⁷

Hofstede subsequently added a fifth dimension to his framework: long-term orientation. This dimension measures the extent to which a society focuses on short or long-term goals.³⁸ Long-term oriented societies favor thrift, persistence, and long-term planning, while short-term oriented societies favor speed, tradition, and enjoying the present.³⁹ Hofstede has assessed only thirty-four cultures on this dimension, with Hong Kong, Japan, and Taiwan displaying high amounts of long-term orientation, and Pakistan and West Africa displaying the lowest amounts.⁴⁰

Hofstede's typology has appeared in so many cross-cultural studies—over 3000 by one count⁴¹—that “scholarship-based-on-Hofstede” has itself become an object of empirical research.⁴² On the other hand, Hofstede's study and results have also faced considerable criticism—some of it scathing⁴³—and other researchers have sought to develop alternatives. A review of the various competing approaches lies beyond the scope of this paper. However, it suffices to observe that many of them, including Shalom Schwartz's Value Dimensions and the Global Leadership and Organizational Behavior Effectiveness (GLOBE) framework, include dimensions very similar to Hofstede's, including those relating to egalitarianism, risk-aversion, and collectivism.⁴⁴ Future research will have to evaluate whether another model would provide more consistent and meaningful results when applied to questions of comparative corporate governance.

³⁷ *Id.* at 286.

³⁸ *Id.* at 69, 351.

³⁹ HOFSTEDÉ, *supra* note 22, at 360.

⁴⁰ *Id.* at 500.

⁴¹ ALBERT JOLINK, SCOREN NAAR BEHOREN, *ECONOMISCH STATISTISCHE BERICHTEN* 158, 158 (2006).

⁴² See, e.g., Bradley L. Kirkman et al., *A Quarter Century of Culture's Consequences: A Review of Empirical Research Incorporating Hofstede's Cultural Values Framework*, 37 *J. INT'L BUS. STUD.* 285 (2006).

⁴³ See Brandon McSweeney, *Hofstede's Model of National Cultural Differences and Their Consequences: A Triumph of Faith—A Failure of Analysis*, 55 *HUM. REL.* 89 (2002). Hofstede responded to McSweeney's critique in Geert Hofstede, *Dimensions Do Not Exist: A Reply to Brendan McSweeney*, 55(11) *HUM. REL.* 1 (2002), available at <http://www.geert-hofstede.com/dimBSGH.pdf>.

⁴⁴ On Schwartz, see HOFSTEDÉ, *supra* note 22, at 264–65; Amir Licht et al., *Culture, Law, and Corporate Governance*, 25 *INT'L REV. L. & ECON.* 229, 235–37 (2005). On GLOBE, see Geert Hofstede, *What Did GLOBE Really Measure? Researchers' Minds Versus Respondents' Minds*, 37 *J. INT'L BUS. STUD.* 882 (2006). The same issue contains a response to Hofstede's article, as well as several other pieces on the increasingly acrimonious Hofstede-GLOBE debate.

II. HOFSTEDE AND COMPARATIVE CORPORATE GOVERNANCE

Until the last decade, surprisingly few scholars attempted to use Hofstede's research to explain the international diversity of corporate governance, perhaps because his work took root in management scholarship and remains little-known among jurists. Over the past ten years, however, a number of pioneering studies have illustrated the potential of Hofstede's framework in this area.

In 1995, Stephen B. Salter and Frederick Niswander explored the relationship between culture and accounting practices in twenty-nine countries and found a number of significant relationships, particularly with the dimension of uncertainty avoidance.⁴⁵ Higher UA countries featured (a) more active government regulation of the accounting profession; (b) less public disclosure of financial data; (c) greater conservatism in accounting methods; and (d) less overall uniformity in accounting practices (a possible consequence of less disclosure).⁴⁶ Salter and Niswander also observed that more individualistic cultures tended to have more disclosure, while more masculine cultures exhibited less conservatism.⁴⁷ The findings suggest that the accounting practices of more masculine, individualistic, and uncertainty-accepting cultures—like the United States⁴⁸—feature greater uniformity, optimism, and disclosure. These factors can encourage more widespread investment in equities and thus development of dispersed shareholding patterns.

Other studies have focused the Hofstede framework on investors. Loek Halman observed that cultures with high levels of power distance showed less faith in the idea of company owners appointing managers.⁴⁹ This finding suggests that these cultures would be less likely to develop the separation of shareholding and management.⁵⁰ Marieke de Mooij found that people in low UA cultures preferred investments in stocks, while those in high UA societies opted for gold and gems.⁵¹ These results suggest that lower levels of

⁴⁵ Stephen B. Salter & Frederick Niswander, *Cultural Influence on the Development of Accounting Systems Internationally: A Test of Gray's [1988] Theory*, 26 J. INT'L BUS. STUD. 379, 388 (1995). Their literature review also refers to two related previous studies. *See id.*

⁴⁶ *Id.*

⁴⁷ *Id.*

⁴⁸ *See infra* Table 3.

⁴⁹ HOFSTEDE, *supra* note 22, at 505 (citing Loek Halman, Waarden, De Westerse Wereld: Een Internationale Exploratie Van de Waarden in de Westerse Samenleving (1991) (unpublished doctoral thesis, Tilburg University)).

⁵⁰ *See infra* Table 3.

⁵¹ HOFSTEDE, *supra* note 22, at 508 (citing Marieke De Mooij, Convergence-Divergence (2001) (unpublished doctoral thesis, Universidad de Navarra)).

uncertainty avoidance would bolster demand for equity and thus contribute to the growth of stock markets.⁵²

The values and motivations of a company's management also impact its corporate governance structure. In 2002, Hofstede et al. surveyed 1800 junior managers and professionals from fifteen different countries and constructed an archetypal chief executive for each culture.⁵³ They found that in cultures with higher power distance the model executive placed a greater value upon power, reputation, and family interest.⁵⁴ This suggests that corporate leaders in such countries may show a greater desire to maintain personal control over a firm and ensure that it remains within their families.⁵⁵ The researchers also observed that the archetypal chief executives in cultures with higher uncertainty avoidance placed less emphasis upon patriotism and national pride, while the executive in those cultures with greater individualism cared less about long-term profits.⁵⁶

Radislav Semenov's doctoral thesis, published in 2000, represented the first attempt to apply Hofstede's cultural model directly to the issue of comparative corporate governance.⁵⁷ Semenov aimed to bridge the gap between cultural, legal, and institutional approaches by identifying "mediating factors" that translated cultural programming into particular facets of corporate governance.⁵⁸ He then applied a regression analysis to eighteen developed Western economies to identify significant relationships between the mediating factors and the cultural dimensions.⁵⁹ Like Salter and Niswander, he found that uncertainty avoidance proved the most significant variable.⁶⁰ Lower UA related to more developed stock markets, lower bank savings, greater regulatory protection for shareholders, shorter employee tenure, and a lower level of public pensions—mediating factors that all supported the emergence of dispersed shareholding and a market for corporate control.⁶¹

⁵² For subsequent evidence in support of this hypothesis, see De Jong & Semenov, *CDFB*, *supra* note 16, § 5.1.

⁵³ See Geert Hofstede et al., *What Goals Do Business Leaders Pursue? A Study in Fifteen Countries*, 33 *J. INT'L BUS. STUD.* 785 (2002).

⁵⁴ *Id.* at 799.

⁵⁵ SEMENOV, *supra* note 12, at 136.

⁵⁶ Hofstede et al., *supra* note 53, at 799.

⁵⁷ See SEMENOV, *supra* note 12.

⁵⁸ *Id.* at 104–54.

⁵⁹ *Id.* at 154–92.

⁶⁰ *Id.* at 179–80.

⁶¹ *Id.*

The following year, Hofstede's model of comparative corporate governance appeared in legal literature.⁶² Amir N. Licht presented both Hofstede's and Schwartz's cultural measurement frameworks and hypothesized about how they may explain certain fundamental features of corporate governance, including relative size of the equity market, concentrated shareholding, prohibitions of self-dealing and insider trading, executive compensation, mandatory disclosure, and hostile takeovers.⁶³ Table 1 summarizes Licht's conjectures.

Table 1: Licht's Hypotheses⁶⁴

Element of Corporate Governance	Hofstede Cultural Variable	<i>A Priori</i> Explanation
Overall Size of Equity Markets	Uncertainty Avoidance (Inverse)	Risk-averse investors have less taste for equity-like investments.
Concentrated Shareholding	Power Distance	Minority shareholders view "second-class" status as a matter of course.
Pyramid Corporations	Power Distance	Pyramid structures seen as a "facet of a proper social order."
Regulations Against Insider Trading & Self-Dealing	Individualism	Small investors require protection for individual initiative.
	Power Distance (Inverse)	Anti-insider trading rules protect the "rank-and-file" parties.
High Executive Compensation	Power Distance	Differences in pay are seen as natural.
Disclosure Rules	Uncertainty Avoidance (Inverse)	Risk-averse corporate stakeholders suppress transparency to avoid conflict and competition.
Hostile Takeovers	Masculinity	
	Individualism	

Licht and his associates have since undertaken to test some of these hypotheses empirically.⁶⁵ In a recent paper that surveyed forty-nine countries, they explored the relationship between culture and the degree of legal protection afforded to creditors and minority shareholders, as quantified by La Porta et al. in the "Creditor Rights Index" and "Antidirector Rights Index."⁶⁶ Uncertainty avoidance emerged as the only significant Hofstede variable, with higher UA related to greater protection for creditors and lower

⁶² See generally Licht, *supra* note 20.

⁶³ See *infra* Table 1.

⁶⁴ See Licht, *supra* note 20. The table excludes a few additional proposed hypotheses based exclusively on Schwartz's cultural dimensions. It bears mention that both of Licht's papers lose some clarity due to the constant shifting between the Hofstede and Schwartz frameworks.

⁶⁵ See Licht et al., *supra* note 44.

⁶⁶ Rafael La Porta et al., *Legal Determinants of External Finance*, 52 J. FIN. 1131, 1134-35 (1997) [hereinafter La Porta et al., *Legal Determinants*]. The Antidirector Index ranked countries from 0 to 5, with one point being awarded for each of the following: (1) possibility of mail-in proxy voting; (2) possibility of voting without previous deposit of shares; (3) legality of cumulative voting; (4) some form of oppression mechanism; and (5) threshold to call an emergency shareholder meeting at or under 10 percent. The Creditor Rights Index ranked countries from 0 to 4, with one point being awarded for each of the following: (1) restrictions on reorganizations; (2) no automatic stay on taking possession of security; (3) debtor relieved of administration during reorganizations; and (4) secured creditors given first ranking on distribution of assets. *Id.*

UA related to greater protection for shareholders.⁶⁷ The results suggest that larger levels of cultural risk-aversion should result in increased preference for debt financing over equity.

In management literature, Trevor Buck and Azura Shahrin have criticized Licht's "piecemeal approach"⁶⁸ and instead have advocated treating a country's entire corporate regime as a unified whole. They outlined the two key regimes of stock market capitalism and welfare capitalism—a dichotomy that appears throughout the corporate governance literature with numerous subtle variations.⁶⁹ Stock market capitalism, found in the United States and the United Kingdom, is characterized by highly dispersed shareholding, hostile takeovers, significant accounting disclosure, shareholder-oriented boards and regulation, and high levels of equity-based executive pay.⁷⁰ Welfare capitalism, found in Germany and Japan, features block shareholding, friendly mergers, secrecy, wider stakeholder involvement in corporate governance, and less reliance on equity-based pay.⁷¹

Buck and Shahrin speculated that low levels of UA coupled with high levels of individualism—as found in the United States and the United Kingdom—would rise to market capitalism, while high levels of UA coupled with collectivism—found in Japan and Germany—would give rise to welfare capitalism.⁷² Concerning the two other permutations, Buck and Shahrin proposed that individualism and high UA, found in France and Belgium, would foster state-influenced capitalism, with "governance structures featuring ownership and control by the State rather than by other stakeholders (e.g., employees or banks) lacking the high Collectivism needed to effect control of managers throughout their voices."⁷³ For countries with the opposite qualities—low UA and high collectivism—they predicted the rise of family-based capitalism with the "small, entrepreneurial family firms" they claimed exemplified the corporate milieu of Hong Kong and Singapore.⁷⁴

Figure 1, below, illustrates how thirty-one of the world's more mature economies fall into the Buck and Shahrin framework. The countries on the scatter plot include all those included in Hofstede's seminal study⁷⁵ whose per

⁶⁷ Licht et al., *supra* note 44, at 241.

⁶⁸ Buck & Shahrin, *supra* note 21, at 44.

⁶⁹ See generally Erik Berglöf, *A Note on the Typology of Financial Systems*, in *COMPARATIVE CORPORATE GOVERNANCE*, *supra* note 6, at 151. For a more recent review of the literature, see Grant & Kirchmaier, *supra* note 4, § 2.

⁷⁰ Buck & Shahrin, *supra* note 21, at 44–46.

⁷¹ *Id.*

⁷² *Id.*

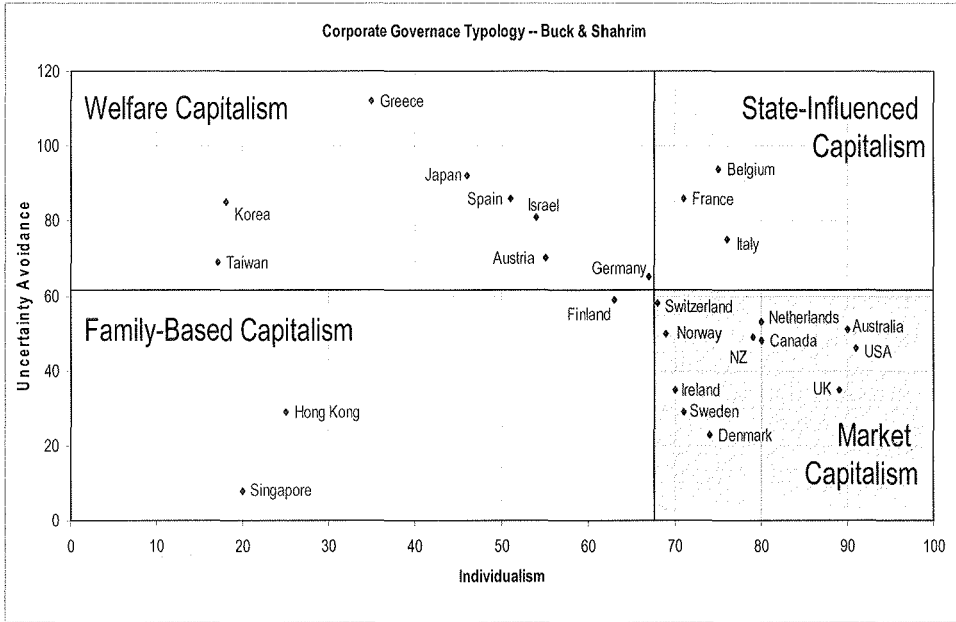
⁷³ *Id.* at 46.

⁷⁴ *Id.* at 45.

⁷⁵ HOFSTEDE, *supra* note 22, at 500.

capita Gross Domestic Product exceeds \$20,000⁷⁶ and whose level of transparency falls above 4 on Transparency International’s Corruption Perceptions Index.⁷⁷ This survey excludes less-developed countries since they typically exhibit less diversity in corporate governance due to reasons extraneous to culture.⁷⁸

Figure 1⁷⁹



Buck and Shahrin made no further effort to justify their typology, and instead focused their empirical inquiry on the narrow question of executive stock options, which Germany had only recently began using for executive compensation. Because Germany was a more collectivist and risk-averse society than the United States and the United Kingdom, Buck and Shahrin hypothesized that Germany’s use of stock options would extend to more

⁷⁶ CIA, THE WORLD FACTBOOK—2006 (2006), <http://www.cia.gov/cia/publications/factbook/index.html> (last visited Oct. 20, 2007).

⁷⁷ TRANSPARENCY INTERNATIONAL, CORRUPTION PERCEPTIONS INDEX—2006 (2006), http://www.transparency.org/policy_research/surveys_indices/cpi/2006 (last visited Oct. 20, 2007).

⁷⁸ In less-developed countries, corporate governance tends to feature concentrated shareholding, corporate groups, and the absence of a market for corporate control. SEMENOV, *supra* note 12, at 278. Gilson has recently proposed that economies should be classified by the amount of corporate diversity they contain. He hypothesizes that countries with effective regulatory regimes should develop an appropriate mix of widespread and concentrated shareholding, whilst those without will invariably tend towards predominantly family-based block control. See Ronald J. Gilson, *Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy* (Stanford L. and Econ. Olin Working Paper No. 309, 2005).

⁷⁹ HOFSTEDE, *supra* note 22, at 500.

managers, involve a smaller proportion of the firm's capital, and contain more numerous and demanding performance conditions.⁸⁰ Their results confirmed these hypotheses vis-à-vis the United States, but not the United Kingdom, whose executive stock option regime was "more German" than Germany's.⁸¹ To explain this surprising finding, Buck and Shahrim suggested that in Great Britain, other forms of executive compensation may fill the role of stock options—an explanation that reinforces the importance of looking at systems as a whole rather than "piecemeal" elements.⁸²

The systems-level analysis that Buck and Shahrim advocated emerged in the research of Eelke de Jong and Radislav Semenov, who studied the impact of cultural difference upon various patterns of shareholding.⁸³ Their most recent work considered the relationship between culture and concentrated shareholding in twenty-seven countries.⁸⁴ Table 2 summarizes their findings:

Table 2: De Jong & Semenov – Link Between Culture & Concentrated Ownership⁸⁵

Intermediate Factors	Measurement Variable	Hypothesized Link to Culture Variables	Results of Regression
Legislative Protector of Minority Shareholders	La Porta's Antidirector Index	Uncertainty Avoidance (Inverse)	Confirmed
		Power Distance (Inverse)	Not Confirmed
Importance of Implicit Contracts	Average Employee Tenure	Uncertainty Avoidance	Confirmed
		Power Distance (Inverse)	Not Confirmed
		Masculinity (Inverse)	Not Confirmed
Stock Market Development	Market Capitalisation / GDP	Uncertainty Avoidance (Inverse)	Confirmed
		Masculinity	Confirmed

Conclusion

Prevalence of Concentrated Ownership	La Porta Ownership Study	Uncertainty Avoidance	Confirmed
		Masculinity (Inverse)	Confirmed

De Jong and Semenov found that power distance and individualism did not correlate significantly with concentrated ownership, contradicting hypotheses advanced by Licht and by Buck and Shahrim.⁸⁶ They propose that

⁸⁰ Buck & Shahrim, *supra* note 21, at 47–50.

⁸¹ *Id.* at 56.

⁸² They also offer the possible explanation that Germany is still in the process of adapting executive stock options and may yet still evolve into a more egalitarian regime than Great Britain's. *Id.* at 58.

⁸³ De Jong & Semenov, *CDOC*, *supra* note 19, at 162. De Jong also has studied the impact of cultural difference upon openness to foreign investment and central bank policy. See Eelke de Jong, *Why are Price Stability and Statutory Independence of Central Banks Negatively Correlated? The Role of Culture*, 18 EUR. J. POL. ECON. 675, 676 (2002); see also Eelke de Jong et al., *Culture and Openness*, 78 SOC. INDICATORS RES. 111 (2006).

⁸⁴ De Jong & Semenov, *CDOC*, *supra* note 19, at 162.

⁸⁵ *Id.* at 161.

⁸⁶ *Id.*

these variables may influence the various mediating factors in different directions and thereby cancel each other out.⁸⁷

In a forthcoming paper, de Jong and Semenov also explore the link between culture and stock market development, as measured by a country's market capitalization divided by its GDP.⁸⁸ Their findings show that countries with higher levels of power distance and masculinity and lower levels of uncertainty avoidance develop larger stock markets.⁸⁹ Surprisingly, they again find no significant relationship between individualism and equity market size.⁹⁰

III. CRITIQUE OF BUCK & SHAHRIM'S MODEL

A closer look at Figure 1 reveals the problems inherent in the Buck and Shahrin typology. The leftward-rising slope of the scatter plot suggests that the two dimensions of uncertainty avoidance and individualism are not independent for the countries in question, arguing against a two-dimensional typology. Moreover, the characterization of Germany as a "collectivist" society seems contrived, since its level of individualism (67) falls much closer to that of France (71) than to that of Japan (46).

The "state-influenced capitalism" category, with only three countries—France, Italy, and Belgium—seems too small to allow for meaningful generalizations. The governments of all three nations do tend to intervene actively in the countries' economies, as evidenced by their scores on Mark A. Miles et al.'s Economic Freedom Index.⁹¹ Although state participation has long constituted a particular hallmark of French and Italian corporate governance,⁹² the government plays a far less overt role in Belgium. State ownership of Belgian public companies is insignificant and corporate governance is characterized by firms grouped in pyramid structures ultimately beholden to key families or foreign enterprises.⁹³ Norway, Singapore, and especially Austria all feature comparable or higher levels of

⁸⁷ *Id.* at 162.

⁸⁸ De Jong & Semenov, *CDFB*, *supra* note 16, at 169.

⁸⁹ *Id.* at Table 3.

⁹⁰ *Id.*

⁹¹ MARK A. MILES ET AL., THE HERITAGE FOUNDATION, 2006 INDEX OF ECONOMIC FREEDOM 13 (2006). The ultra-conservative political agenda of the Heritage Foundation no doubt colors the Economic Freedom Index. Further research may develop more objective indicators of state participation in corporate governance.

⁹² On France, see Grant & Kirchmaier, *supra* note 4, at 21–22. See generally Melowar & Mott, *supra* note 4. On Italy, see Grant & Kirchmaier, *supra* note 4, at 22.

⁹³ Eddy Wymeersch, *Holding Companies in Belgium*, in *COMPARATIVE CORPORATE GOVERNANCE*, *supra* note 6, at 67–68, 87.

government shareholding, even though they fall outside of Buck and Shahrim's "state-influenced capitalism" zone.⁹⁴

Consistent with Buck and Shahrim's hypothesis, corporate control in Hong Kong is highly concentrated in leading families.⁹⁵ However, numerous other countries outside the "family-based capitalism" zone also feature highly concentrated family control, including Taiwan,⁹⁶ Korea,⁹⁷ and Israel.⁹⁸ Key families feature prominently in Singapore's corporate milieu; however, the country also features a conspicuous amount of state shareholding, with "almost a quarter (23 percent) of its companies state-controlled."⁹⁹ The cases of Belgium and Singapore illustrate that family and state control may complement, rather than oppose, each other, particularly if the country's leading families have close ties with government officials.

Buck and Shahrim's "market-capitalism" quadrant also includes the Scandinavian countries, whose corporate regimes have more in common with Germany and even France than with Anglo-American countries. No Scandinavian country has developed the dispersed shareholding¹⁰⁰ or shareholder-centered regulatory framework¹⁰¹ that characterize the classical market-based model.

Looking at all four quadrants, therefore, it seems clear that the Buck and Shahrim typology fails to accurately classify the world's industrialized countries in terms of their dominant corporate governance regimes. This can change, however, with one relatively simple revision.

IV. A REVISED MODEL

As discussed previously, de Jong and Semenov found that masculinity, not individualism, correlates significantly with the growth of stock markets and the development of dispersed shareholding.¹⁰² Figure 2 illustrates how the typology changes after making this substitution:

⁹⁴ La Porta et al., *Corporate Ownership*, *supra* note 8, at 492–95.

⁹⁵ Claessens et al., *supra* note 10, at 83–84.

⁹⁶ *Id.* at 82, 101.

⁹⁷ *Id.* at 83–84.

⁹⁸ Beni Lauterbach & Alexander Vaninsky, *Ownership Structure and Firm Performance: Evidence from Israel*, 3 J. MGMT. & GOVERNANCE 189, 192 (1999), available at <http://www.biu.ac.il/soc/sb/fac/stfhome/lauterbah/publications/28.pdf>.

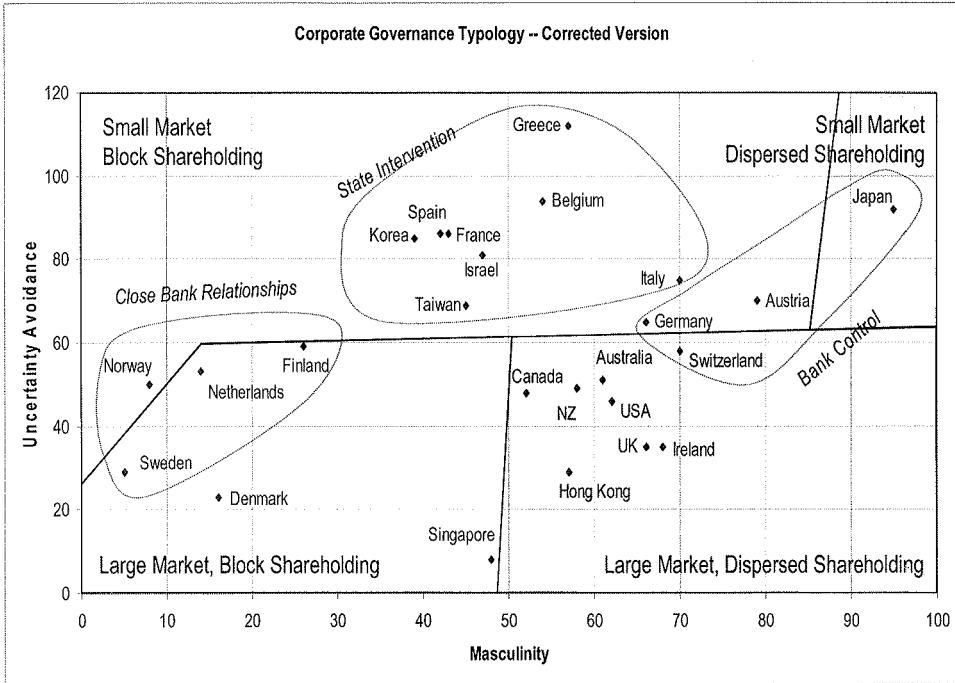
⁹⁹ Claessens et al., *supra* note 10, at 103. See also Haider A. Khan, *Corporate Governance in Singapore and Hong Kong: What Can the Other Asian Economies Learn?* 12–16 (June 2003) (unpublished manuscript, available at <http://www.e.u.-tokyo.ac.jp/cirje/research/dp/2003/2003cf229.pdf>).

¹⁰⁰ See *infra* Table 3.

¹⁰¹ As evidenced by their respective scores on the Antidirector Index. See generally La Porta et al., *Legal Determinants*, *supra* note 66.

¹⁰² See *supra* Table 2.

Figure 2¹⁰³



A number of indicators, summarized in Table 3, below, facilitate the evaluation of the revised typology, including:

- **Stock Market Development:** The average of 2001–2005 year-end stock market capitalization divided by GDP.¹⁰⁴ Development over 100 percent is classified as “high,” and development below 100 percent is classified as “low.”

¹⁰³ Data from HOFSTEDÉ, *supra* note 22, at 500.

¹⁰⁴World Bank, World Development Indicators, <http://ddp-ext.worldbank.org/ext/DDPQQ/member.do?method=getMembers&userid=1&queryId=135/>, except for Taiwan’s, which comes from the Taiwan Stock Exchange, http://www.tse.com.tw/en/statistics/statistics_week.php (last visited Nov.20, 2007)[hereinafter Taiwan Stock Exchange]. Note that Taiwan’s percentage is for 2005 only.

Table 3: Summary of Indicators¹⁰⁵

Country	Hofstede Cultural Dimensions				Market Development (Market Cap./GDP)		Dispersed Shareholding (% of Companies)		Government Intervention (Econ. Freedom)		Close Bank Relationship or Control
	PD	IDV	MAS	UA							
Austria	11	55	79	70	24%	Small	3%	Block	1.95	Low	High
Belgium	65	75	54	94	98%	Small	13%	Block	2.11	Low	Low
France	68	71	43	86	80%	Small	30%	Block	2.51	High	Low
Germany	35	67	66	65	45%	Small	30%	Block	1.96	Low	High
Greece	60	35	57	112	63%	Small	5%	Block	2.80	High	n.a.
Israel	13	54	47	81	71%	Small	8%	Block	2.36	High	n.a.
Italy	50	76	70	75	45%	Small	10%	Block	2.50	High	Low
Norway	31	69	8	50	49%	Small	23%	Block	2.29	Low	High
South Korea	60	18	39	85	60%	Small	43%	Block	2.63	High	Low
Spain	57	51	42	86	81%	Small	18%	Block	2.33	High	Low
Taiwan	58	17	45	69	140%	Large	n.a.	Block	2.38	High	n.a.
Top-Left Quadrant	46	53	50	79	69%	Block	18%	Block	2.35	High	
Top-Right Quadrant (Japan)	54	46	95	92	73%	Small	60%	Dispersed	2.26	Low	High
Denmark	18	74	16	23	58%	Small	35%	Block	1.78	Low	Low
Finland	33	63	26	59	115%	Large	28%	Block	1.85	Low	High
Netherlands	38	80	14	53	108%	Large	20%	Block	1.90	Low	High
Singapore	74	20	48	8	150%	Large	28%	Block	1.56	Low	Low
Sweden	31	71	5	29	100%	Large	18%	Block	1.96	Low	High
Bottom-Left Quadrant	39	62	22	34	106%	Large	26%	Block	1.81	Low	
Hong Kong	68	25	57	29	425%	Large	5%	Block	1.28	Low	Low
Australia	36	90	61	51	108%	Large	48%	Dispersed	1.84	Low	Low
Canada	39	80	52	48	107%	Large	60%	Dispersed	1.85	Low	Low
Ireland	28	70	68	35	60%	Small	57%	Dispersed	1.58	Low	n.a.
New Zealand	22	79	58	49	39%	Small	44%	Block	1.84	Low	Low
Switzerland	34	68	70	58	233%	Large	55%	Dispersed	1.89	Low	High
United Kingdom	35	89	66	35	136%	Large	80%	Dispersed	1.74	Low	Low
United States	40	91	62	46	130%	Large	85%	Dispersed	1.84	Low	Low
Bottom-Right Quadrant	38	74	62	44	186%	Large	54%	Dispersed	1.73	Low	
Correlations											
PD	1.00	-0.52	0.09	0.25	0.37				-0.12		0.23
IDV		1.00	-0.03	-0.18	-0.27				0.42		-0.23
MAS			1.00	0.28	0.06				0.30		-0.05
UA				1.00	-0.36				-0.29		0.83

• **Dispersed Ownership:** The percentage of large and medium-sized companies (averaged together) without a 20 percent (direct or indirect) controlling shareholder, based on the findings of Rafael La Porta et al.¹⁰⁶ It bears note, however, that some of these findings may no longer be valid,

¹⁰⁵ Data from HOFSTEDE, *supra* note 22, at 500; World Bank, World Development Indicators, *supra* note 104; Taiwan Stock Exchange, *supra* note 104; La Porta et al., *Corporate Ownership*, *supra* note 8, at 492, 494; Tsun-Siou Lee & Yin-Hua Yeh, *Corporate Governance and Financial Distress: Evidence from Taiwan*, 12 CORP. GOV. 378, 386 (2004); De Jong & Semenov, *CDFB*, *supra* note 16, § 4.6; SEMENOV, *supra* note 12, at 24-31; MILES ET AL., *supra* note 91.

¹⁰⁶ La Porta et al., *Corporate Ownership*, *supra* note 8, at 492, 494. It bears note that some of La Porta's observations have become dated; Spain, for example, has developed more widespread ownership subsequent to a large-scale privatization initiative in the late 1990s. Grant & Kirchmaier, *supra* note 4, at 3.

particularly in the emerging markets. Countries with dispersed ownership proportions over 45 percent were classified as “dispersed” (or high), and countries with less than 45 percent were classified as “block” (or low). Taiwan, not included in La Porta’s study, received a ranking of “block” based on other sources.¹⁰⁷

- **Bank Control:** Whether banks participate actively in the supervision and governance of public corporations or have particularly close relationships with their client firms. The classification follows de Jong and Semenov (2005) and Semenov (2000) for the Western economies,¹⁰⁸ and Khan for the Asian economies.¹⁰⁹ However, it bears note that the three studies were considering different aspects of firm-bank relationships and their classifications may not be perfectly analogous. The classifications of Israel, Ireland, Greece, and Taiwan—the evidence surrounding which was inconclusive—will be left for further research. Note that significant bank control does not necessarily correspond with large bank equity stakes. For example, Semenov classified Austria and Switzerland as “bank control” economies even though bank shareholdings in both countries are insignificant.¹¹⁰

- **Economic Freedom Index (EFI):** The degree to which the state intervenes in the economy in ways that constrain economic choices by businesses and consumers, as assessed annually by Miles et al.¹¹¹ Scores above 2.3 are classified as “high.”

Figure 2 reveals four distinct zones of differing corporate governance. The Green Zone (top left) contains countries with high uncertainty avoidance and all but the most extreme levels of masculinity. All of these countries feature block shareholding, and all except Taiwan have relatively small stock markets. Most of these countries also feature high levels of state intervention in the economy.

The characteristics of the Green Zone coincide with Licht’s conjectures and de Jong and Semenov’s findings. Higher UA orients investors away from equity investments, entrepreneurs away from selling controlling interests in their firms, and managers away from higher-risk, higher-return projects. All of these factors reduce stock market growth. Higher UA also creates an increased appreciation of stability and thus fewer changes in management,

¹⁰⁷ See, e.g., Tsun-Siou Lee & Yin-Hua Yeh, *supra* note 105, at 386.

¹⁰⁸ De Jong & Semenov, *CDFB*, *supra* note 16, § 4.6; SEMENOV, *supra* note 12, at 24–31. Where the two sources disagree (as they do for Norway and the Netherlands), the former is given priority. Note that the two studies were not discussing exactly the same thing; de Jong & Semenov were looking at the *closeness* of the firm-bank relationship, while Semenov was looking at the degree of bank *control*.

¹⁰⁹ Khan, *supra* note 99, at 6 (Japan, Hong Kong, and South Korea), 32 (Singapore). Note that Khan focused on the issue of *control* rather than the *closeness* of the firm-bank relationship.

¹¹⁰ La Porta et al., *Corporate Ownership*, *supra* note 8, at 492–95.

¹¹¹ MILES ET AL., *supra* note 91.

which fosters block shareholding. Increased state involvement in the economy likewise flows from a general desire for a broader safety net and more market predictability. Taiwan's disproportionately large stock market makes it the only outlier in the Green Zone. However, its large market capitalization may reflect the influence of mainland Chinese investors, whose much lower uncertainty avoidance (30) falls outside of the Green Zone.¹¹²

The Yellow Zone (bottom left) contains countries with low uncertainty avoidance and low masculinity, and includes the Netherlands, Sweden, Denmark, Finland, and Singapore. With one exception, all of the countries in this zone feature large stock markets and block shareholding, which conforms to expectations. As discussed above, low UA orients a firm's various stakeholders towards equity finance, which bolsters stock market development. At the same time, however, their low masculinity steers them to the long-term relationships that characterize block shareholding and away from the hostile takeovers and potentially acrimonious shareholder actions that epitomize dispersed shareholding.

Culture also explains why Denmark, the one anomalous country in the Yellow Zone, has failed to develop a large stock market. De Jong and Semenov also found a significant relationship between power distance and stock market growth,¹¹³ and Denmark has by far the lowest power distance (12) of all the countries studied. The country's extremely low power distance seems to have overcome the effect of low UA and left the country with low market capitalization.

The Red Zone (bottom right) contains countries with high masculinity and low uncertainty avoidance, and includes Switzerland, Hong Kong, and most of the "Anglo" nations including the United States. All of these countries have developed an investor-friendly regulatory regime (scoring 4 or 5 on the Antidirector Index)¹¹⁴ and feature relatively little government intervention in the economy. All but three of the Red Zone countries (Hong Kong, Ireland, and New Zealand) have evolved large stock markets with dispersed ownership. These results are also consistent with Hofstede's framework. As discussed above, lower levels of UA foster the growth of large equity markets. At the same time, higher levels of masculinity result in a more assertive, competitive, and materialistic culture. This can foster shareholder activism, broad public interest in finance, hostile takeovers, managers who value their independence, and other essential elements of a dispersed shareholding regime.

Power distance readily explains the three anomalous countries. Ireland and New Zealand have the lowest levels of power distance in the zone (22 and 28, respectively), which seems to have slowed the growth of their equity

¹¹² HOFSTEDE, *supra* note 22, at 502.

¹¹³ De Jong & Semenov, *CDFB*, *supra* note 16, Table 3.

¹¹⁴ La Porta et al., *Legal Determinants*, *supra* note 66, at 1137.

markets. At the opposite extreme, Hong Kong's high PD (68) may have impeded the development of dispersed shareholding, since it makes shareholders less willing to delegate power to managers and entrepreneurs less willing to relinquish the status and privilege that comes with controlling a firm. Although de Jong and Hofstede failed to find a statistical link between power distance and dispersed ownership,¹¹⁵ their regression may have been diluted by the large number of feminine and high UA countries that tend not to develop dispersed shareholding even under the best of circumstances.

The Purple Zone (top right) contains only Japan, with its highly masculine yet risk-averse culture. Japan has developed an exceptional combination of a relatively small equity market (the hallmark of high uncertainty-avoidance) with dispersed ownership (the hallmark of high masculinity). Although the country produced a number of illustrious corporate raiders during the turmoil of the post-war reconstruction period, Japan eventually evolved a form of dispersed ownership without the shareholder activism and market for control that generally accompanies it.¹¹⁶ The separation of shareholding from control has left Japan's managers accountable to themselves within their own firms and to their peers within their *keiretsu* corporate network.¹¹⁷ Also important is that banks exercise significant influence over corporate governance, in contrast to the Red Zone.¹¹⁸

Figure 2 also reveals three "islands": one island of countries with conspicuous amounts of state intervention in the economy and two islands of countries where banks have special relationships with their client firms. The state-intervention island consists of countries with high UA and moderate levels of masculinity. The existence of this island suggests that people in more risk-averse countries will tend to expect their governments to protect and assist them from misfortune, and these popular desires and expectations can translate into a more activist state. However, since state regulation has the potential to suppress the masculine values of competition and wealth-creation, a more masculine society may seek alternative risk-reduction mechanisms, such as those offered by private financial institutions. Consequently, the state-intervention island gives way to a bank-control island as masculinity increases. The second bank island appears among the most feminine countries. However, in this island, it seems that banks maintain close relationships with their firms, but not necessarily with the degree of overt control seen in the masculine bank islands. Further research may develop a more robust typology of bank-firm relationships and explore its connection to national culture.

¹¹⁵ De Jong & Semenov, *CDOC*, *supra* note 19, at 162.

¹¹⁶ Morck & Nakamura, *supra* note 2, at 69–71.

¹¹⁷ ROE, *supra* note 2, at 179–82.

¹¹⁸ K. MIYASHITA & D. RUSEEL, *KEIRETSU* 44–53 (1996).

The global table of correlations (in grey) also reveals two broad relationships between culture and corporate governance. At least a 95 percent confidence level, uncertainty avoidance significantly correlates with state intervention in the economy, while power distance correlates with market size.

V. POLICY IMPLICATIONS: CONVERGENCE AND DEVELOPING ECONOMIES

The increasing globalization of trade and finance has led to numerous initiatives to harmonize corporate and securities laws around the world. Regulatory convergence reduces the information costs of transnational commerce, which can offer enormous savings to firms in all the countries involved. However, if a society's optimal system of corporate governance varies according to its culture, convergence imposes costs in the form of sub-optimal regulation. For example, the disclosure required to monitor a block shareholder may differ from that required to monitor independent management, and therefore a country's optimal disclosure regime will depend on the relative prevalence of block and dispersed shareholding. A one-size-fits-all regime will result in superfluous disclosure in some places and insufficient disclosure in others, creating unnecessary reporting or agency costs.¹¹⁹

Although the benefits of global regulatory uniformity might well outweigh the aggregate costs of sub-optimal regulation, it seems more likely that there is some optimal mix of harmonized and jurisdiction-specific regulation.¹²⁰ The question of where to draw this line lies beyond the scope of this paper. However, recognition that culture legitimately affects where the line should be drawn represents a significant challenge to certain currents of legal and economic wisdom.¹²¹

Recognition that different countries can have different optimal corporate governance structures affects international development strategy. A developing country cannot expect to implement a comprehensive corporate and securities regime overnight, and cultural factors can indicate where best to set priorities. If the culture's degree of power distance, uncertainty

¹¹⁹ These costs will, in general, be borne disproportionately by economically weaker countries with less influence over the international standard-setting.

¹²⁰ Licht, *supra* note 20, at 152–57.

¹²¹ For example:

Culture is often considered to be one of the powerful environmental factors affecting the accounting system of a country. Additionally, nationalism leads to an unwillingness to follow other countries' accounting practices and to give up sovereignty. These national variations in accounting standards create vast inefficiencies, impede the flow of capital and complicate cross-border transactions at the most basic levels.

Jei-Fang Lew, *The Trend of International Accounting Harmonization*, 10 J. APPLIED MGMT. & ENTREPRENEURSHIP 126, 131 (2005).

avoidance, and masculinity bode the development of a large stock market with dispersed ownership, it may prove most effective to foster the development of equity markets, an independent accounting profession, and investment intermediaries like pension funds. If, however, a country appears more culturally predisposed to smaller markets with block shareholding, regulatory initiatives should focus more on the banking sector or creditor protection.

For example, South Africa's cultural profile suggests it to be an ideal candidate for the development of a large stock market with dispersed ownership. Its relatively low uncertainty avoidance (49) and high masculinity (65) places it firmly in the Red Zone, and its power distance (49), although relatively high for that quadrant, still places the country much closer to the United States than to Hong Kong.¹²² Indeed, South Africa has already developed an enormous stock market (234 percent of GDP in 2005, up from 118 percent in 2001),¹²³ and the six family-controlled conglomerates that dominated the apartheid-era economy have spun off and restructured hundreds of businesses since 1994, reducing the concentration of power in their hands.¹²⁴ South Africa's regulatory regime, which scored a 4 on La Porta et al.'s Antidirector Index,¹²⁵ reflects its equity-orientation. Unlike the developed Red Zone countries, however, the South African government continues to intervene significantly in the economy (EFI of 2.74).¹²⁶

Although the enormous disparities between the country's ethnic groups demand the government's attention, the state may do best by focusing its industrial policy on fostering a business-friendly environment rather than more direct forms of intervention. For example, the Organization for Economic Co-operation and Development has identified South Africa's rigid labor regime—with centralized wage-setting and severe limits on the employment of foreign specialists—as one area where less rigid regulation could reap dividends in forms of increased productivity and lower unemployment.¹²⁷

Malaysia, on the other hand, lies in the Yellow Zone, with low uncertainty avoidance (26) and moderate masculinity (50).¹²⁸ Along with its exceptionally high power distance (104),¹²⁹ these cultural qualities should

¹²² HOFSTEDE, *supra* note 22, at 500.

¹²³ World Bank, World Development Indicators, *supra* note 104.

¹²⁴ Neo Chabane et al., *The Changing Face and Strategies of Big Business in South Africa: More Than a Decade of Political Democracy*, 15 *INDUS. & CORP. CHANGE* 549, 553–58, 573 (2006).

¹²⁵ La Porta et al., *Legal Determinants*, *supra* note 66, at 1137.

¹²⁶ MILES ET AL., *supra* note 91, at 13.

¹²⁷ DONALD KABURAKA & LOUKA T. KASTELI, *AFRICAN ECONOMIC OUTLOOK 2005/2006* 469–70 (2006), available at <http://www.oecd.org/dataoecd/12/8/36748748.pdf>.

¹²⁸ HOFSTEDE, *supra* note 22, at 500.

¹²⁹ *Id.*

promote the growth of its equity markets but limit the growth of dispersed ownership. This has been, thus far, the exact trend in Malaysia, whose stock market stood at 139 percent of GDP in 2005,¹³⁰ but where corporate control has remained concentrated in the hands of key families and, to a lesser extent, the government.¹³¹ As in the case of South Africa, state intervention in the economy rises far above that seen in developed Yellow Zone countries (EFI of 2.98).¹³² This suggests that greater economic freedom may constitute a meaningful middle-term goal. Furthermore, if concentrated shareholding is destined to remain the norm, the country may seek to focus its regulatory initiatives on reforms specifically aimed to prevent abuses of authority by the controlling block-holders, such as increasing the mandatory number of independent directors.¹³³

The cultural dimensions of Chile, which boasts one of Latin America's most sophisticated investment environments, place the country in the Green Zone.¹³⁴ As one would expect from a country in this quadrant, Chile has developed an "insider" system of corporate governance, with control concentrated in the hands of key families and companies organized into corporate groups.¹³⁵ A particular hallmark of Chilean corporate governance is the supervision exercised by the country's private pension funds, which manage assets totaling over half of the country's GDP.¹³⁶ Rather than aspire to develop a system of dispersed shareholding, policy discourse in Chile has focused more on how to improve the supervision exercised by the funds. For example, regulatory changes in 2000 provided greater powers to minority shareholders, and the Central Bank has recently discussed proposals to allow the funds to underwrite bond issues and take larger equity stakes than currently allowed.¹³⁷

Although Green Zone countries tend to gravitate toward more state intervention, the Chilean government plays a relatively small role in managing the economy. As the Central Bank recently remarked, "[a]t present, for good or for ill, the government has no industrial policy."¹³⁸ This suggests

¹³⁰ World Bank, World Development Indicators, *supra* note 104.

¹³¹ Claessens et al., *supra* note 10, at 82, 103.

¹³² MILES ET AL., *supra* note 91, at 13.

¹³³ Gilson, *supra* note 78, at 1656.

¹³⁴ HOFSTEDE, *supra* note 22, at 500.

¹³⁵ Agosin & Pastén, *supra* note 11, at 4–5, 12 (insider system); Marisale Santiago-Castro & Cynthia Brown, *Corporate Ownership Structure and Expropriation of Minority Shareholders' Rights: A Latin American View* 11 (Univ. Tex. Pan Amer. Dep't of Econ. & Fin., Working Paper Series, Nov. 2006), available at <http://www.coba.panam.edu/faculty/jocka/Workingpapers/WORKING%20PAPERS/wp1106.pdf> (corporate groups).

¹³⁶ Agosin & Pastén, *supra* note 11, at 2.

¹³⁷ *Id.* at 7–8.

¹³⁸ *Id.* at 2.

that, unlike South Africa, Chile may benefit more from new and improved state initiatives rather than from deregulation. For example, the OECD has written approvingly of the government's public-private infrastructure initiatives and has called for the state to centralize and improve, rather than abolish, its National Innovation System.¹³⁹ Finally, although Green Zone countries tend to have small stock markets, Chile's stood at 118 percent of GDP in 2005.¹⁴⁰ Chile's stock market capitalization has grown enormously over the past several years, perhaps due to large foreign inflows of capital. However, the country still has a low per capita GDP (U.S. \$11,900 in 2005)¹⁴¹ that may reduce the weight of its stock market to levels more typical of Green Zone countries as it grows.

Although no other countries in Hofstede's original study fall into the Purple Zone, subsequent research has suggested that Hungary shares Japan's unusual combination of high masculinity (88) and high UA (82).¹⁴² Thus far, however, Hungary has failed to develop a regime of dispersed shareholding. Its percentage of publicly listed firms without a block-holder actually fell from 11 percent to 6 percent between 1996 and 2000.¹⁴³ However, as would be expected in a Purple Zone country, its banking sector has done relatively well compared with its peers.¹⁴⁴ State involvement in the economy remains high (EFI of 2.44),¹⁴⁵ and the persistent inability of the government to meet its spending targets continues to attract criticism.¹⁴⁶ If and when financial and political pressures obligate the state to scale back its economic policy, banks may come to play an important role in the supervision of Hungarian corporations. Hungary may, therefore, do best to concentrate its regulatory reform efforts on the development of its banking sector in order to facilitate the growth of its banks into institutional monitors of the firms with which they do business. When this happens, the block-holdings may gradually unwind and more dispersed ownership may emerge.

VI. CONCLUSION: LOOKING AHEAD

The fact that culture can have legitimate impacts upon corporate governance calls into question the very purpose of a corporation. It appears

¹³⁹ OECD, ECONOMICS DEPARTMENT, POLICY BRIEF: ECONOMIC SURVEY OF CHILE—2005 (2005), available at <http://www.oecd.org/dataoecd/4/13/35540886.pdf>.

¹⁴⁰ World Bank, World Bank Development Indicators, *supra* note 104.

¹⁴¹ CIA, *supra* note 76.

¹⁴² HOFSTEDE, *supra* note 22, at 502.

¹⁴³ Éva Ozsvald, *Corporate Governance in Hungary—An Overview*, in CORPORATE GOVERNANCE IN TRANSITION ECONOMIES—PART II: THE CASE OF HUNGARY 1, 9 (Ichiro Iwasaki ed., 2005).

¹⁴⁴ *Id.* at 6.

¹⁴⁵ MILES ET AL., *supra* note 91, at 13.

¹⁴⁶ OECD, ECONOMICS DEPARTMENT, POLICY BRIEF: ECONOMIC SURVEY OF HUNGARY—2005 1, 3 (2005), available at <http://www.oecd.org/dataoecd/9/0/35105097.pdf>.

that cultures constitute their corporations in such a way that collectively maximizes the utility of the *society as a whole*, responding to the degree of uncertainty avoidance, masculinity, and power-distance not only of their shareholders, but also managers, employees, creditors, and other stakeholders. The fact that corporations organize themselves to suit the needs of *all* their stakeholders belies the principle of shareholder primacy, which enthrones a firm's shareholders as its "owners" and makes the maximization of *their* wealth the *raison d'être* of its existence. At the very least, shareholder primacy may itself be a highly culturally-dependent assumption that should not be taken for granted in international corporate governance discourse.

The scholar of modern anthropology will also notice that the four quadrants of Figure 2 correspond to Ronald L. Jepperson's classification of how cultures organize their polities.¹⁴⁷ The top left corresponds to the *Latin* (statist-associational) polity, the bottom left to the *Nordic* (communal-corporatist), the bottom right to the *Anglo* (communal-associational), and the top right to the *Germanic* (statist-corporatist).¹⁴⁸ Further research can explore how these distinct polities give rise to different corporate governance regimes. For now, it suffices to observe that insofar as culture affects a country's perception of its *polity*, so should it also color its conception of institutions—like corporations—which rely on political action for their very existence, purpose, and legitimacy.

The values and motivations of management, in particular, play a significant role in the setting of corporate priorities, and may lead to the adoption of courses of action that may place shareholder interests behind those of other stakeholders. David A. Waldman et al., for example, recently found that in cultures with lower levels of power distance and higher levels of institutional collectivism¹⁴⁹ managers showed greater orientation towards corporate social responsibility, particularly towards non-shareholder stakeholders.¹⁵⁰ Their findings suggest that stakeholder theory—the view of the corporation that regards it as more than a vehicle for maximizing shareholder wealth—may have greater currency in less hierarchical and more collectivist societies, such as Austria and Israel.

A corporation does not exist outside the minds of the individuals who collectively will it into being. Its existence is rooted in laws and governance

¹⁴⁷ See Ronald L. Jepperson, *Political Modernities: Disentangling Two Underlying Dimensions of Institutional Differentiation*, 20 SOC. THEORY 61 (2002).

¹⁴⁸ See generally SEMENOV, *supra* note 12, at 25–31.

¹⁴⁹ Several researchers have suggested that Hofstede's dimension of "individualism-collectivism" is too general. The GLOBE framework, used by Waldman et al., considers "institutional-level collectivism" and "in-group collectivism" as two separate dimensions of cultural difference. David A. Waldman et al., *Cultural and Leadership Predictors of Corporate Social Responsibility Values in Top Management: A GLOBE Study of 15 Countries*, 37 J. INT'L BUS. STUD. 823 (2006).

¹⁵⁰ *Id.* at 832.

structures that endow it with personality and allow it to manifest itself in society. Since the corporation is inherently a social construct, its conception, justification, and governance structure depend on the particular values and aspirations of the society that constructs it. Ultimately, greater awareness of the impact of culture upon corporate governance has the potential to reshape discussion of international finance. In addition to challenging widely-held notions of shareholder primacy and the benefits of regulatory convergence, the impact of culture illustrates the danger of applying terminology such as “shareholder rights,” “ownership,” “oppression,” or “fiduciary duty”—terms devised in one particular legal and cultural context—to discussions of corporate governance in another. Adequately incorporating cultural difference into policy initiatives will help ensure that the world’s corporate governance regimes advance the interests of the world as a whole, rather than just Western investors.

