UC Berkeley
Political Economy of International Finance

Title

Restructuring “Germany Inc.”: The Politics of Company and Takeover Law Reform in Germany and the European Union

Permalink
https://escholarship.org/uc/item/4p15c19g

Author
Cioffi, John W.

Publication Date
2002-04-15

eScholarship.org Powered by the California Digital Library
University of California

Working Paper PEIF-1

Restructuring "Germany Inc."
The Politics of Company and Takeover Law Reform in Germany and the European Union

by

John W. Cioffi

April 15, 2002

Abstract

The reform of German company law by the Control and Transparency Law ("KonTraG") of 1998 reveals politics of corporate governance liberalization. The reforms strengthened the supervisory board, shareholder rights, and shareholder equality, but left intra-corporate power relations largely intact. Major German financial institutions supported the reform's contribution to the modernization of German finance, but blocked mandatory divestment of equity stakes and cross-shareholding. Conversely, organized labor prevented any erosion of supervisory board codetermination. Paradoxically, by eliminating traditional takeover defenses, the KonTraG's liberalization of company law mobilized German political opposition to the EU's draft Takeover Directive and limited further legal liberalization.

John W. Cioffi, Assistant Professor, Political Science, University of California, Riverside.

I.Introduction

Byestablishingtheinstitutionalstructureofthecorporation,companylawformsthecore ofanycorporategovernancesystem. Whatmakescorporategovernanceanimport antareaof policyandtheoryisitsintermediationoftheprimarythreecorporateconstituencies — shareholders,managers,andemployees. [1]Inanerainwhichstate -ledintermediationappearsto bereceding,corporategovernanceregimesperformsanincreasi nglyimportantintermediation functioninthecoordinationofopposingpoliticalconstituenciesandbodiesofregulation. Companylawinparticularplaysacentralroleinthisprocessbymediatingthecompeting demandsoffinancialmarketlawandregulat ionandlaborrelationslaw.Thepoliticsof securitiesregulationpitmanagersagainstshareholders(andotherholdersoffinancialassets) overissuesoftransparency,disclosure,andrulesgoverningparticipationinthecapitalmarkets. Thepoliticsoflaborrelationsprimarilyentailsaperennialbattlebetweenmanagersand organizedlaborovertherulesgoverninglabororganization,collectivebargaining,andthe representationofemployeeinterestswithinthefirm.Theseareasthusinvolvedifferen tsetsof interestgroupsinconflictoverdifferentsalienteconomicandnormativeissues.Theresulting divergentpoliticaldynamicsincreasetheriskthatthesebodiesoflaw,andthepoliciesthey embody,willconflictwitheachotheraschangesinoneareaarenotmatchedbycorresponding andcomplementarychangesintheother.Thepoliticalsystemandadjudicationinthecourts coordinatetheseareasimperfectlyatbest.Bycreatingthebasiccorporatestructurethat integratesthesethreeconstitu encies,companylawplaysacrucialmediatingrolebetweenthe normsofsecuritiesregulationandthoseoflaborrelationslawandtherebycontributestothe systemiccoherenceessentialtobothadynamicandcompetitiveeconomyandafunctionallegal system.

ThispaperanalyzestherecentevolutionofGermancompanylawasacasestudyofhow thisareaoflawreflectsthepoliticalstrugglesovertheformofthecorporationandcorporate governanceandhowitsdevelopmentreconcilesopposinginterestsan dotherwisedivergentlegal structures.TheanalysisfocusesonthepoliticsthatresultedinthepassageoftheControland

[1] *See*Cioffi,200a, *cf.*Cioffi,2000b.

TransparencyAct(the“KonTraG”)in1998 [2]—theonlymajorreformofGermancompanylaw since1965 —andhowthenewstructureofcomp anylawreflectsthetensionbetweensecurities marketdevelopmentandneo -corporatistlaborrelations.Thepaperthenconsidershowthe KonTraGreconstitutedtheinterestsofGermanpoliticalandeconomicelitesindomesticand Europeanpolitics.Byren deringGermanfirmsmorevulnerabletohostiletakeovers,the KonTraGandrelatedtaxreformlegislationgalvanizedoppositiontofurtherliberalizationand shareholder-friendlyreforms.Asaresult,Germanoppositiontoencroachingneo -liberalism spearheaded,inrapidsuccession,theultimatedefeatoftheEUTakeoverDirectiveandthe successfulefforttoadoptadomestictakeoverlawthatsanctionedmorepotentanti -takeover defensesinJuly2001.

ThenegotiationanddraftingoftheKonTraGshowshow politicsdrivesthedevelopment ofcompanylawanditsreconciliationoftheconflictinginterestsofshareholders,managers,and employees.Thepoliticsofcompanylawreformwaspulledintwodifferentdirections.First,the legislativereformwasthe productofintenseinterestgroupcompetitionforpowerwithinfirm governance(andtherentsthatcomewithit)andfueledbypopulistfearsofconcentrated financialpower.Second,companylawperformsthecrucialpoliticaleconomicfunctionof reconcilingthedemandsofsecuritiesregulationsandlaborrelationslaw —andtheinterestsof thedifferentclustersofconstituenciesmostkeenlyinterestedintheseareasoflawand regulation—whilefashioningareasonablyefficientstructureforthecorporate form.Failurein satisfyingthisfunctionwoulderodetheutilityofthecorporateformitselfandrenderthe corporategovernancesystemdysfunctionalasdifferentareasoflawmadeincompatibledemands onthecorporation.Thepoliticssurroundingthea doptionoftheKonTraGindicatesthatthe populistresentmentsofconcentratedfinancialpowerweremanipulatedforpartisanpolitical gain,butdidnotdeterminethesubstanceofthelegalreform.TheKonTraGwastheproductof eliteinterestgrouppolit icsandthetechnicalexpertiseofprofessionalswithinthefederal ministries,thepeakassociations,andindustry.ThemoderatesintheSPDandthethen -ruling CDU-ledcoalitionfashionedthetermsofthepoliticaldealsthatmadethelawpossibleandt he MinistryofJusticesuppliedthetechnicalexpertisethattransformedthedealsintolegislation. Theprocessoflegalchangedependednotonlyonthestructuralandinterestgrouppressures

[2]CorporateControlandTransparencyAct(GesetzzurKontrolleundTransparenzimUnternehmensbereich, KonTraG)of27April1998,Fede ralLawGazette,PartI,p.786(Gesetzvom27.4.1998,BGBl.I,S.786vom 30.4.1998).

generated within the financial sector and the labor relations system, but also on entrepreneurial state actors seeking reform for their own political and ideological ends. However, as subsequent EU and domestic developments show, these reforms unleashed a host of unintended consequences that constrained later efforts by the SPD (by then in power) and the European Commission to liberalize company law and corporate governance.

In Germany, company law reform implicated the conflict between the conceptions of shareholder value and shareholder supremacy in Anglo-American shareholder capitalism and corporate governance, and Germany's post-war commitment to the neo-corporatist stakeholder conception of the firm and the social market economy. This clash gave rise to a debate over the definition and arrangement of legitimate interests within corporate governance and decision-making. The resolution of this debate in the context of company law reform had to satisfy the intensifying demands for securities market modernization[3] and more stringent, shareholder-protective regulation, as well as normative commitment to effective employee representation on supervisory boards under codetermination law. The KonTraG legislation reconciled these countervailing demands by fostering greater transparency, shareholder democracy, and accountability in corporate governance without altering the core legal duties of directors or the structure of the supervisory board under codetermination.

Once amended and reformed, the new company law framework substantially reshaped the interests of management, labor, and shareholders with respect to corporate governance. Financial market reform and legislation had been closely related to the EU's programmatic commitment to the integration of European capital markets. This modernization program had met with only partial success in the absence of substantial changes in company law. The KonTraG was seen as necessary to advance the modernization of securities markets in Germany by lowering the risks of owning shares by small shareholders. Ironically, the initial liberalization brought about by the passage of the KonTraG ultimately doomed the further liberalization of takeover law. The law also exposed German corporations to greater takeover vulnerability in an emerging European market for corporate control. The KonTraG (along with subsequent tax reform legislation) deprived German managers of the use of "golden shares" and cross-shareholdings that had long served as anti-takeover defenses. This set in motion a conflict over

[3] *I.e.*, the development of the regulatory infrastructure to facilitate the increased securitization of finance and the move away from bank-centered finance.

the Takeover Directive in the EU in which the German government and European Parliamentarians argued that the measure favored the firms of some member states over others. The German members of the European Parliament mobilized opposition from other national contingents to defeat the Takeover Directive. Immediately thereafter, the Germany passed its first takeover law, not to protect shareholders but to legally sanction American-style anti-takeover defenses. The rejection of the Takeover Directive by the European Parliament ended over twelve years of tortuous negotiations among the member states and was the first time a major policy initiative of the European Commission had been thwarted by Parliament. The adoption of the protective German Takeover Law entrenched the commitments of German political and economic elites against further liberalization of corporate governance that has been a core concern of EU integrationists. This complicated story reveals both the divisive domestic political battles triggered by corporate governance reform and their increasingly important international political implications.

II. Origins of the KonTraG: The Structural Problems in German Company Law

A. Crisis of Confidence: The German Corporate Governance Model in the 1990s

By the mid-1990s a crisis of confidence was growing in Germany.[4] The country was running persistently and unsustainably high unemployment rates, economic growth was anemic, the integration of the former East Germany had stalled badly and triggered a severe recession, and some observers believed that many of the country's firms and the economy as a whole were losing their innovative capacity and competitive edge. Further, a series of serious corporate scandals had erupted throughout the early and mid-1990s that suggested deeper systemic problems in Germany's bank-centered corporate governance regime.[5] For example, Metallgesellschaft AG nearly collapsed from previously undisclosed debts despite the fact that Deutsche Bank, Dresdner Bank, and Commerzbank were all substantial shareholders and were expected to monitor the firm's affairs.[6] Likewise, when Daimler Benz AG chose to list its

[4] For the following general observations on the German economic and political situation in the late-1990s, I am indebted to many German interviewees whom I spoke to in the summer, autumn, and winter of 1999, and the summer of 2000. Prof. Dr. Marcus Lutter, one of Germany's leading company law scholars, was particularly helpful in placing the corporate governance and company law reforms into historical context. Interview, Prof. Dr. Marcus Lutter, University of Bonn, Department of Law, Bonn, November 31, 1999.
[5] *See*, *e.g.*, Gordon, 2000: 5-6; Ziegler, 2000: 203-204; Wenger and Kaserer, 1998a: 41-78; Wenger and Kaserer, 1998b: 499-536.
[6] Gordon, 2000: 5-6.

AmericanDepositaryReceiptsontheNewYorkStockExchangeitrestateditsfinancesunder AmericanGenerallyAcceptedAccountingPrinciples(USGAAP)andsudd enlydisclosedovera billiondollarsinlosseswhenithadpreviouslyreportedahealthyprofitunderGerman accountingrules.InthesubsequentscandaltheformerCFOcommittedsuicide.This extraordinaryfinancialreversalwasnotdisclosedpriortot heswitchtoUSGAAPdespitethe factthataDeutscheBankrepresentativewasthechairmanofDaimler'ssupervisoryboardand thebankownedovertwentypercentofthecompany.

Tomany,thesescandalsrevealedthefailuresoftheGermancorporategoverna nce regime'srelianceonbankstomonitorfirmsandtheirmanagers.Manyamongthegeneral public,andespeciallythoseonthepoliticalleft,therecurrentfinancialscandalssuggestedthat thebanksthemselveswereexploitingconflictsofinterestbyus ingtheircentralpositionin corporategovernancetoensurerepaymentofloansratherthantoprotectshareholderinterests. Infact,itisextremelydifficulttotellwhattheroleofthebankswasinthesescandals —whether theywereill -informedoract ingintheirownconflictedself -interest—becausethecorporate governancesystemandfinancialdisclosurerulesintheearly1990syieldedsuchanopaque imageoffirmfinancesandaffairs.ButtheopacityofcorporateGermanyservedtointensify popularsuspicionsoftheeffectivenessandfundamentalfairnessoftheGermansysteminthe shadowoftheserecurrentfinancialscandals.

DevelopmentsinEuropeanandinternationalcapitalmarketsalsopromptedea reassessmentoftheGermancorporateGovernance regime.TheEUhadbegunarevolutionary attempttoharmonizeandintegratememberstates'securitiesmarketsthroughaseriesof financialservicesdirectives.ThepervasivefeelingofuneaseabouttheGermaneconomicmodel grewthroughoutthedecadea stheGermaneconomycontinuedtostumblewhiletheUnited Statesbegananextraordinaryeconomicboomdrivenbysecuritiesmarketsandthefinancingof newtechnologies.Atthesametime,theinternationalcorporategovernancemovementspread throughout theadvancedindustrializedworldduringmostofthe1990sascapitalmarketsgrew moreintegratedandinvestmentfundsspannedtheglobeseekinginvestmentopportunities.The traditionalGermanfinancialmodelofstrongbanks,undevelopedsecuritiesmark ets,andweak minorityshareholdershadbeguntolookanachronistic.Opaquefinances,poorfinancial disclosure,feebleandpassivesupervisoryboards,andweaklegalrightsandremediesavailable toshareholdershadledtolowlevelsofsecuritizedfinan ce,financialandmanagerialrisk

aversion,andfirmgovernanceonbehalfofinsiders(managers,controllingshareholders,and creditorbanks).

Thelowlevelsoftransparencyincorporatefinancespervadedthe *internal*governanceof thefirmaswell.The weaknessofthesupervisoryboardanddominanceofthemanagement boardvirtuallyensuredlowlevelsoftransparency.Managementcontrolledtheauditingand disclosureoffirmfinances.Theimbalanceofpowerbetweensupervisoryandmanagement boardswas sogreatthatmanagersengagedinafairlycommonpracticeofprovidingsupervisory boardmemberswiththeauditor'sreportonthecorporation'sfinancesatthemeetinginwhich theyweretoapproveit —andthencollectthereportattheendofthemeeting topreservethe confidentialityoftheinformationitcontained.Thispracticeeffectivelykeptthefirm'sfinances confidentialfromthesupervisoryboardaswellandresultedintherubber -stampingofthe accounts.

Inaddition,thelaw(andstockexc hangerules,unlikethoseoftheNYSE)permittedthe useof"goldenshares,"dualclasssharevotingrights,andvotingcapsthatenabledadominant shareholderorshareholdergrouptowieldcontroloveracorporationwithoutputtinga commensurateamount ofcapitalatrisk.Shareholderinequalityfurtherdiscouraged shareholdingbyprospectiveinvestors.Thesevotingstructurespreservedthecontroloffounding familiesanddominantshareholders,butatthepriceofshareholderdemocracyandattherisk that thecorporationwouldberunonbehalfofthesecontrollinginterestsandthatrentswouldbe divertedfromshareholdersasawholetoaclassofinsiders.Aspolicymakers,financiers,and scholarsbecameincreasinglyinterestedindevelopingtheef ficiencyandutilizationofsecurities markets,thesearrangementshavebeencriticizedfortheireconomicallyinefficientdiversionof resourcesandforrenderingsecuritiesriskierandlessprevalentasamodeofsaving,investment, andfinancing.

Germancompanylawdeprivedmanagersofanumberofmodernfinancialtoolsthatcan beusefulinimprovingshareholdervalueandcorporatefinancialperformance.Inparticular,the companylawprohibitedcorporationsfromrepurchasingtheirownsharesandpla cedsubstantial restrictionsontheabilityofthefirmanditsmanagerstoissuenewsharesandoptions.The inabilitytorepurchasesharesdeprivedfirmsofameansofincreasingshareholdervalueby raisingtheratioofcapitalpershareoutstandingan dfurtherentrenchedincentivestoretain earningsforinefficientactivitiesbydeprivingmanagersofawaytoincreaseshareholderwealth

without the double taxation incurred by paying dividends (a tax on the firm's income as it earns a profit, and a second tax on individual income when a dividend is paid).

Finally, supervisory board codetermination exerts a fundamental impact on the structure and operation of the board in corporate governance. At the very core of corporate governance, supervisory board codetermination precludes the development of a clear normative hierarchy such as that represented by the concept of shareholder primacy. The Codetermination Act of 1976 grants employee representatives half the board seats in firms with over 2,000 employees and one third of the seats in firms with 500 to 2,000 employees.[7] Codetermination legitimates at least two sets of interests — those of the shareholders and those of employees — that must be reflected in the law's conception of directors' fiduciary obligations. As a result, outside of the most egregious misconduct it is difficult to fashion a framework of fiduciary duties that can define clear standards for the conduct of the director's office. Moreover, critics charged that supervisory boards (particularly of major corporations) were too large and unwieldy to engage in effective deliberation or efficient decision-making. The presence of employee representatives on supervisory boards encouraged, and to some degree mandated, the enlargement of the board to make room for them. Critics also argued that employee representation discouraged the development of more active boards. More powerful and informed supervisory boards would empower employees and unions as much as they would shareholders — thus reducing the incentives for shareholders and their representatives on the board from becoming more active.[8] Court rulings in codetermination cases effectively prohibited the formation of board committees of directors (*e.g.*, audit or finance committees (akin to those comprised of outside directors in American corporate governance) that systematically excluded employee representatives. While these rulings protected codetermination and its commitment to a form of economic democracy, they also precluded one principal means of addressing conflicts of interests and collective action problems deriving from the large board size. By the mid-1990s, protecting shareholders and increasing the use of securitized finance had become important policy goals. Political elites began to craft reform agendas to promote modernization of the German economy, while economic elites sought to increase returns on capital and improve the dynamism and competitiveness of the German corporation.

---

[7] Codetermination Act (*Gesetz uber die Mitbestimmung von Arbeitnehmern*) of May 4, 1976 (BGBl. I 1153), as amended October 28, 1994 (BGBl. I 3210) ("MitbestG").
[8] *See*, *e.g.*, Roe, 1998; Pistor, 1998.

B.ProblemsintheHousebankModel

Duringthe1980s andearly1990s,aschoolofthoughtemergedtoutingtheadvantagesof theGermanbank -centeredfinancialandgovernancemodelonthegroundthatitprovideda mechanismforthemonitoringanddisciplineofcorporatemanagerswhilesupplyingstablelong - termfinance. [9]Underlyingthisclaimwasthetheory(orassumption)thattheGermanfinancial systemalignedtheinterestsofstrong,centralized,andwell -representedfinancialinstitutions withthoseofindividualshareholders.ThissanguineviewofGer mancorporategovernance erodedduringthe1990s.

Recentempiricalresearchindicatesthatbanksactprimarilyasdebt -holders,whichmeans thattheirinterestsdonotalignwiththoseofshareholders. [10]Hence,bankinfluenceover corporategovernance,e ventotheextentitexists,maygiverisetoavarietyofconflictsbetween thebanksandothershareholders.Mostoftheseconflictsstemfromthefactthatbanksgenerally actasdebt -holdingcreditorsfirstandshareholderssecond.Thebanks’primary interestsin corporategovernancearegenerallythepaymentofinterestonloansandtherecoveryof collateralintheeventofcorporatecollapse. [11]Moreover,PeterMülberthasshownhowlarge Germanuniversalbanksuselong -termequitystakesinclient firmstostabilizetheirearnings streamsandbuttresstheirdeposittakingandlendingbusiness. [12]Becausethebanksseekstable, ratherthanmaximized,earningsinordertomaintaintheconfidenceofdepositors,theirinterests conflictwiththoseofoth ershareholdersandtheycannotberelieduponto monitormanagement intheshareholders’collectiveinterest.

Mülbert’sanalysissuggeststhatGermanymaysoonwitnessasubstantialreconfiguration ofcorporategovernanceinfavorofshareholderinteres tsasmajorbanksshifttheirbusiness modelsfromtraditionaldeposit -takingrelationalfinancetowardsgreaterrelianceonsecurities tradingandinvestmentbankingservices. [13]Thischangemay,inturn,increasepressuresfor

---

[9] *See*, *e.g.*,Albert,1993;Roe,1994,1993;Streeck,1992,1991 *seealso* Soskice,1999;LazonickandO’Sullivan, 1997;1992; *cf*.Porter,1990;Zysman,1983.

[10] *See*Mülbert, 1998.

[11]Thecontroversyoverbankconflictsofinterestsisoflong -standing. *See*Vagts,1966:57 -58.Inacrisis,abank mayseektoreduceitsloanexposurebycuttingoffcreditorcallingpriorloansdueeventhoughsuchactionsmay pushafirminto bankruptcy.Abankalsomayhaveaninterestinwithholdingfinancialinformationfromthepublic inordertoraisemorecapitalfromshareholderstoprotectitscapital.Thesepotentialconflictsofinterestare weaknessesoftheGermanmodel.

[12]Mülbe rt,1998; *seealso* Deeg,1999.

[13]ThisanalysistakesonincreasedimportancenowthattheGermanfederalgovernmenthaspassedtaxlegislationto encouragethebankstoliquidatetheirequityholdings.

short-term increases in profits and return on equity.[14] Increased competitive pressures on the big German universal banks suggest that the banks will have to modernize their operations and business models.[15] Ongoing reform of securities law and regulation since the early 1990s formed one dimension of legal and institutional infrastructure needed for this shift. Company law reform constituted the second dimension. Yet, because of the multiple interests mediated by company law, reform of this legal area proved more difficult than that of securities law. The most difficult of these interests to accommodate in company law reform were those of organized labor.

C. The Symbolic Politics of Supervisory Board Codetermination

Supervisory board codetermination remains a defining feature of German corporate governance and a significant constraint on the development of shareholder capitalism in Germany along Anglo-American lines. Principles of shareholder primacy and the economic theory of corporate governance as a principal-agent relationship between shareholders and managers lead to an analytical focus on the board and the degree to which it protects and maximizes shareholder interests. Not surprisingly, substantial attention has been lavished on the exceptional level of employee representation on the supervisory boards of major German corporations as part of a debate over codetermination's efficiency, effects on share and/or firm performance, and normative justifications. As Anglo-American theories of the firm, finance, and corporate governance made their way among intellectual and policy circles in Europe and specifically in Germany, they provided additional ammunition in a long-running debate over board codetermination.[16]

Many, if not most, businessmen, attorneys, labor leaders, and others involved in corporate governance in Germany minimize the importance of supervisory board

[14] *Cf.* Mülbert, 1998: 485-486. However, different institutional forms taken by equity investment also alter the interests of shareholders in terms of time horizons for returns and appetite for risk. A mutual fund faces far more intense pressures for immediate returns than a pension fund with a stable (*i.e.*, locked-in) pool of capital and an investment and payout horizon of twenty-five years. Thus, conflicts between shareholder value and patient capital do not necessarily conform to the distinction between debt and equity. Germany therefore may be able to preserve patient capital within its own emerging and distinctive form of shareholder capitalism.

[15] *See* Breuer, 1998: 542.

[16] This debate over the economic, legal, and normative dimensions of board codetermination has gone on as long as the institutional arrangement has existed. Following the enactment of the Codetermination Law of 1976, German firms and business associations brought a landmark suit to hold the statute unconstitutional. *See Codetermination Case*, 50 BverfGE 290 (1979), European Commercial Cases, vol. 2, pp. 324-386 (1979) (challenging the constitutionality of the Codetermination Act (Gesetz uber die Mitbestimmung von Arbeitnehmern) of May 4, 1976 (BGBl. I 1153), as amended October 28, 1994 (BGBl. I 3210) ("MitbestG").

codetermination.[17] This relative indifference to supervisory board codetermination derives from the political impossibility of repealing or scaling back employee representation, as well as a widespread understanding that codetermination does not impose significant costs on German firms. The available evidence suggests that the focus on the impact of codetermination on the board's functioning is misplaced. Just as the board is not a particularly effective institutional form for firm governance and the monitoring of management, codetermination of the board appears to have had at most a modest impact on the operations and governance of major German corporations. Some commentators have argued that codetermination impedes takeovers and rapid organizational changes that might harm employee interests, thus bringing about an alliance of managers seeking to entrench themselves and employees guarding against threats to employment security and redistribution to shareholders.[18] Corporate restructuring and legal reforms since the mid-1990s to date call this alleged function of codetermination into question.[19] Indeed, notwithstanding the presence of labor on the supervisory board, German firms have been able to restructure and retrench, and these moves have often been accompanied by significant downsizing of the workforce. For example, during the late 1990s corporate giants such as Daimler Benz and Deutsche Telekom shed tens of thousands of employees as their business and financial positions deteriorated. Downsizing in Germany is far more likely to be accomplished through attrition and early retirement packages, rather than the harsher and more rapid layoffs common in the United States. Yet the *works council*, rather than the employee representatives on the supervisory board, plays the dominant role in protecting employee interests in corporate restructuring situations.[20] The marginal import of supervisory board codetermination has contributed to the path dependence of the institutional form. No significant interest group gains or loses much on account of board codetermination.

During the mid to late-1990s, organized labor and the center-left in Germany shifted their attitudes towards shareholder value and finance capitalism. Senior labor leaders came to understand the limits of power and influence that supervisory board codetermination bestows

---

[17] This was the uniform impression received from numerous interviewees in law, business, labor relation, policy makers, and academics. For a superb review of the literature on supervisory board codetermination, and other subjects relating to the structure and operation of the German corporate board, *see* Prigge, 1998.
[18] Roe, 1998.
[19] *See* the discussion of the Mannesmann hostile takeover case in this paper, *infra*.
[20] Supervisory Board may actually facilitate restructuring and limited downsizing by providing employee representatives, including the head of the works council, with sufficient information on the state of the business to justify drastic measures.

uponemployees.Duringthe1990s,itbecameincreasinglyclearthattheriseofglobal finance, thepushtomodernizeGermancapitalmarkets,andtheincreasingpresenceofAnglo-American shareholderswouldfurtherdiminishtheimportanceandusefulnessofboardcodetermination. Duringthelate-1990s,leadersoftheSPD'sdominantcentrists,ledbyGerhardSchröderand lieutenantssuchasHansMartinBury,begantoadvocatethesemodernizationattemptsand modifiednotionsofshareholdervalue —withappropriatecheckstocurtailtheperceivedexcesses ofAmerican"casinocapitalism" —asaneconomicplankoftheirNeueMitteprogram.Officials atthetopofthelabormovementcametoacceptthevalidityandpotentialbenefitsofthesenew economicprinciplesandcapitalmarketreforms.Bytheendofthe1990sagrowingnumberof seniorunion officialsandtheirpolicyadvisorsconcededthattheGermaneconomycouldusethe greaterdynamism,managerialdiscipline,andfinancialflexibilitysuppliedbytheincreased availabilityofsecuritizedfinance.[21]Thisledtotheconcomitantconclusionthatthesupervisory boardwouldtendtoprotectshareholderinterestsmorevigorouslyinthepastandthatitwould losemoreofitsalreadymodestvaluetoemployees.

However,boardrepresentationretainswidespreadpublicsupportandsubstantial symbolicpowerwithinGermanpolitics,andallinterestgroupsrecognizethatanyattemptto eliminateorsignificantlyrollbackcodeterminationwouldunleashapopularbacklashacrossthe politicalspectrum.[22]Thecontinuedsymbolicimportanceofboardcodeterminationis particularlypotentamongtherankandfileoftheindustrialunionsandwithintheleftwingofthe SocialDemocraticParty.[23]AsMarkRoehasdescribedit,boardcodeterminationisoneofthe "sacredcows"ofGermanpolitics.[24]Theunionsand SocialDemocratscannotaffordtoalienate theirbasesbynegotiatingoverthesubject,despiteagrowingrealizationattheseniorlevelsof thelabormovementandtheSPDthatitislosingitssignificanceandalreadylimitedutilityto

---

[21]AnonymousinterviewswithGermanlaborunionofficials,summer1999,winter1999,andsummer2000.Itis noteworthythattheseofficialswereconsistentlyunwillingtobeidentifiedwiththispositionbecauseofits sensitivitywithinthelabormovementandthehostilityoftherankandfiletoshareholderinterestsandfinance capitalismgenerally.

[22]Interviews,Dr.RainerFunke,MemberoftheBundestag,FDPBundesfraktion,Berlin,November2,1999;Otto Fricke,AttorneyatLawandCounselor,FDP,Berlin,November1,1999.Thisfearofpoliticalbacklashagainst companylawreformsthatcompromisecodeterminationalsooperatesatthelevel oftheEuropeanUnion.Interview, PeterM.Wiesner,HeadofLegalAffairs,Legal,CompetitionPolicy,andInsuranceDepartment,Federationof GermanIndustry(BDI),Brussels,Berlin,July11,2000.

[23]Thispointwasrepeatedlymadebytoo manyintervieweestolistindividually.Thelegitimacyandpopularityof boardcodeterminationandanticipationoffiercepoliticalandindustrialresistancetoeffortstoweakenorenditis simplytheacceptedpoliticalandsocio-economicstateofaffairsinGermany.

[24]Roe,1998; *seealso* Pistor,1998.

labor. Thus, symbolic politics has locked into place an institutional form that has little effect on the actual distribution of power and resources.

No major corporate stakeholder (management, labor, banks, and shareholders or their representatives) has been willing to expend the political capital and incur the political risks required to alter codetermination on the supervisory board. The rhetoric surrounding the issue has been both heated and lofty, but in reality the political stakes are too high and the economic stakes too low to allow for any significant legal and institutional change.[25] On the political right, employers and the more liberal-leaning political conservatives are unwilling to pay the political and potential economic price of challenging codetermination. Even the Free Democratic Party (the FDP), Germany's small neo-liberal party, has refrained from any significant attacks on the institution of board codetermination. When they had their best chance to alter the practice, during the final years of the Kohl government's Christian Democrat-Free Democrat coalition, they saw no reason to provoke a battle over codetermination that might jeopardize more important and urgently needed reforms of securities and company law. Corporate managers did not have an interest in refashioning the supervisory board as a more effective disciplinary and oversight mechanism and thus did not press for changes in codetermination. Finally, like the Free Democrats, financial interests led by the large universal banks did not savor the prospect of political combat over changes in codetermination rules and sought major reforms of securities laws and markets that fostered their interests through increased transparency and market liquidity, and were content to restrict company law reforms to those that left codetermination untouched.

III. The Control and Transparency Act (KonTraG)

In contrast with the United States, German company law is the exclusive province of federal law. Consequently, company law reform culminated in a centralized legislative process at the federal level that produced the KonTraG. The reform aimed at facilitating the transition from a bank-centered financial system to a more securities-driven model. It also supplied the preconditions for sweeping federal tax reform legislation in the autumn of 2000 that took direct aim at the web of bank-centered cross-shareholdings among German corporations that has defined "Germany Inc." throughout the post-war era. At the same time, the KonTraG

[25] Interview, Prof. Dr. Theodor Baums, University of Osnabrück, Osnabrück, July 13, 1999.

maintainedtheestablishedbalance ofpowersamongmanagerial,employee,andshareholder interestsstoagreaterextentthanintheUnitedStates.Countervailingpoliticalpressuresduring thestruggleforcompanylawreformensuredthatcodeterminationremainedundiminishedbythe KonTraG.Theresultwasarathermodestreformthatstrengthenedthepositionofthe supervisoryboardinrelationtothatofthemanagementboardwhileincreasingfinancial transparencyandmanagerialaccountability.TheKonTraGdidnot,however,embrace shareholderprimacy,nordiditsignalthetriumphofAmerican -styleshareholdercapitalismin Germany.[26]

A. BashingBanksandObliqueLiberalization:PoliticalEntrepreneurialism, EconomicModernization,andtheSPD'sProposedLegislation

TheKonTraGwastheb rainchildofTheodorBaums.OneofGermany'sfinestyoung legalacademicsandlongavociferousadvocateofcorporategovernancereform,heapproached HansMartinBury,anup -and-comingmemberoftheSPDintheBundestag,topitchanideato putgovernanc ereformonthenationalpoliticalagenda. [27]Baumsenvisionedalegislative strategythatwouldplaywellwiththeleft -wingoftheSPD,wouldhelpestablishtheSPDasthe partyofeconomicmodernization,andhaveareasonablechanceofdeliveringbenefic ial

---

[26]ThestructureoffederalismintheUnitedStatesrelegatescompanylawprimarilytothesphereofstatelegisl ation, whilethefederalgovernmenthastakentheleadroleinsecuritiesregulationandlaborlaw.Thelong -established legalandpoliticalpracticeofthecharteringandstructuringofcorporationsunderstatelaw,thepatternsoffederal regulationfoc usingonsecuritiesandlabormarketsratherthantheinternalstructureofthecorporation,andSupreme Courtdoctrinevindicatingthelatitudeofstatelegislationinorderingcorporateaffairshavepreservedthecentrality ofstatelawintheinternalg overnanceofcorporations.Withinthisfederaliststructure,therelativepoliticaland economicstrengthofmanagerialinterestsagainstbothorganizedlaborandshareholdersgavemanagersadecisive advantageindeveloping(andlitigating)anti -takeoverdefensesanddraftingstateanti -takeoverlawsthatco -opted theinterestsofemployeeswhilegivingthemnoroleinfirmgovernance.Americantakeoverdefenseswere sanctionedbythecourts,includingthoseinDelaware,withinhighlycomplex —andfrequen tlyunstable —judicially createddoctrinesthatsoughttobalancethepowersofmanagerstoexercisetheirbusinessjudgmentintheconduct offirmaffairsandtochangecorporatechartersandby -lawswithfiduciaryobligationstoshareholders.Anti - takeoverstatuteswerethemorehighlypoliticizedresponsetotheupheavalswroughtbythehostiletakeoverera. Takenoutofthedeliberativeandtechnicalcontextofthecourts,legislationdesignedtocurbtakeoversreflected anti-financierpopulismthaten abledmanagerialelitestomobilizelaborandthepublicatlargeagainstshareholder interestsasrepresentedbyfinancialinstitutionsandothersinvolvedinhostiletakeovers.Thelegislativeoutcomes consistentlyembodiedabalanceofinterestgroupp owerinstatepoliticsthattiltedsubstantiallytowards management.Asaconsequence,themostprevalentformofanti -takeoverlegislation,the"corporateconstituency law,"allowedmanagerstotakeemployeeinterestsintoaccountwhenrespondingtoaho stiletakeoverbid,butgave employeesnovoiceinfirmgovernanceeveninthecontextofatakeoverbattle.ForanoverviewoftheAmerican hostiletakeovermovementandpoliticalandlegalresponsesthereto, *see*Alcalay,1994;Wallman,1990,1991; *see also*essayscollectedinBlair,1993;Bhagat,Shleifer,andVishny,1990;ShleiferandVishny,1990.Thepresence ofpopulistresistancetoconcentratedandpowerfulfinancialelitesisconsistentwithRoe'shistoricalanalysis(1991) oftheroleplayedby anti -financierpopulismintheshapingthedistinctiveU.S.financialmarketstructureduringthe 19thand20 thcenturies.

[27]Interview,Prof.Dr.TheodorBaums,UniversityofOsnabrück,Osnabrück,July13,1999.

companylawreformsthatthelong-rulingCDU-CSUhadresistedforyears.[28] HesuggestedthattheSPDproposethefirstmajorlegislativereformofthecountry'scompanylawsince1965bytargetingexcessivebankpowerinthefinancialandcorporategovernance.Byattackingthebigbanks,theSPDwouldmaintainthesupportofitsleftwingandtheunions.Thepartycouldmobilizeaformofanti-financierpopulismthathadbeensmolderingalreadyasaresultoffinancialscandals.TheSPDhierarchysawthisasanopportunitytodemonstratethatthepartywasseriousaboutrestructuringtheeconomy,whileportrayingtheCDU-CSUasperpetuatingthecozyinsulatedfinancialandcorporaterelationshipsthatnolongerappearedtobeservingGermanysowell.

ThedraftlegislationintroducedbytheSPDintheBundestagmandatedthedivestmentofthebanks'equitystakeincorporations,imposedalimitoffiveboardmandates(seats)perperson,andthetotalprohibitionofbankvotingofshareproxies.TheSPDdraftalsofavoredregulationthatgavetheBAKred,Germany'sfederalbankregulator,expandedauthoritytoinvestigatetheactivitiesofbanksincorporategovernance.AccordingtoBaums,heandtheSPDsponsorsoftheproposedlegislationknewthatthedrafthadabsolutelynochanceofpassageandhadconstructedittosetupabargainingpositionthatwouldproducefinallegislationthatwouldreformcorporategovernancewithoutalienatingthebigbankstothedegreethattheywouldmobilizetokillthelegislation.Thestrategywastogetpublicattentionandpressurethegovernmenttosupportacompromisebillthatwouldbefarlessradical,butstillusefulinimprovingcorporategovernance.[29] Thestrategyworked.[30]

---

[28] Theneo-liberalFDP,theCDU-CSU'scoalitionpartnerduringtheKohlgovernment,hadsoughtsomemeasureofcompanylawreformtobenefitshareholderinterestsformuchofthe1990sbuthadbeenrebuffedandendlesslydelayedbythemoretraditionalistCDU.Thegoverningcoalitionhadsetupaworkinggrouponcompanylawreform,buttheCDUmadenoseriousefforttoaddresstheissuesofcorporategovernanceandcompanylawreformuntiltheSPDproposalwasmadepublic.Interview,Dr.RainerFunke,MemberoftheBundestag,FDPBundesfraktion,Berlin,November2,1999.ForascholarlydiscussionoftheroleandinfluenceoftheFDPandneo-liberalideasoncompanylawreform, *see* Ziegler,2000:203-204.

[29] Interview,Prof.Dr.TheodorBaums,UniversityofOsnabrück,Osnabrück,July13,1999.

[30] Threedevelopmentsrevealtheextraordinarysuccessofthispoliticalandlegalstrategy.First,thereisthesuccessfulpassageoftheKonTraGreformlegislation—eveninitsultimatecompromiseform—discussedbelow.Second,Hans-MartinBurybecameoneofthepre-eminentSPDpoliticiansofhisgenerationandoneofChancellorSchröder'sprincipallieutenantsintheChancelleryasaStaatsminsterandBundeskanzlerafterthepartycametopower.Third,TheodorBaumsroseinprominenceandinfluenceinparallelwiththerisingfortunesofSchröder,Bury,andtheSPD.HehasbecomeoneofSchröder'smostimportantlegaladvisorsandtheheadofthegovernment-sponsoredCorporateGovernanceCommission(popularlyknownastheBaumsCommissionandonwhichBuryplayedaprominentrole)chargedwithreviewingthepracticeandlegalstructureofGermancorporategovernanceandsubmittingproposalsforreform. *See GermanLawJournal*,July16,2001; GovernmentCommissiononCorporateGovernance(BaumsCommission) PressRelease,June21,2000; Jahn, 2001;

B. Interest Group Politics and Parliamentary Compromise

Under pressure from the left and from the FDP within its own coalition, the CDU threw its support behind a compromise law. Although the Bundesrat also had worked on a company law reform bill, under German law the upper house has no veto over issues of company law and thus played virtually no role in the legislative process. Ranier Funke of the economically liberal FDP headed the Bundestag committee that handled the bargaining over the terms of the compromise legislation and worked with Ulrich Seibert, a company law expert and the senior official responsible for drafting the legislation in the Ministry of Justice.[31] The banks and the BDB (“Bundesverband deutscher Banken,” the banks’ peak association), demanded substantial tax concessions in the event that they were forced to liquidate their equity holdings.[32] In addition, they stated plainly that their voting of proxies was an increasingly unprofitable service for their brokerage clients and that if the law made this process any more expensive and complex they would simply cease to provide it.[33] In the absence of a substitute for the voting of proxies by the banks, the withdrawal of the banks from this function would result in even fewer shareholders participating in corporate decision-making and more unpredictable shareholder votes.[34] The CDU and FDP politicians involved in the legislative process had thought that the bank power debate was merely populist rhetoric.[35] The banks called the politicians’ bluff, as anticipated by all sides. Neither the government nor the SPD was willing to risk a direct and bitter conflict with the banks, nor were they in a position to advocate a vastly more complicated

---

Government Commission on Corporate Governance, *German Corporate Governance Code* (Draft, dated December 12, 2001).

[31] By a quirk of bureaucratic jurisdiction, the Ministry of Justice has control over the preparation and drafting of company law legislation, while the Ministry of Finance handles these responsibilities in the area of banking and securities market law. In practice, however, this is a small group of talented professionals who often consult with each other when addressing issues that relate to each other's substantive areas of legislation in order to gain access to valuable expertise and to prevent conflicts among the ministries.

[32] Interview, Dr. Ulrich Seibert, Leiter des Referats für Gesellschaftsrecht und Unternehmensverfassung, Ministry of Justice, Berlin, July 5, 1999. They would receive these tax breaks two years later without the compulsory divestment.

[33] *Id*.

[34] Bank proxy voting thus solves a collective action problem in corporate governance. Representatives of the Deutsches Aktieninstitut (DAI), an organization set up by the Deutsche Börse and its members to advance the development of shareholding and securitized finance in Germany, estimated that without bank voting of proxies only 10% to 15% of individual shareholders would vote at the AGM. To avoid the unpredictability of voting under conditions of such low turnout, firms, banks, and most policymakers concur that the bank’s role cannot be abolished without some replacement. Interviews, Markus Herdina, Deutsches Aktieninstitut, Frankfurt, December 6, 1999; Helmut Achatz, Deutsches Aktieninstitut, Frankfurt, December 6, 1999.

[35] Interview, Dr. Rainer Funke, Member of the Bundestag, FDP Bundesfraktion, Berlin, November 2, 1999.

anddivisivetaxreformagendathatwouldbenefitthebanks.[36] ThegovernmentandBundestag agreedtoremovetheprovisionsmostobjectionabletothebanksandbusiness,inparticularthe compulsorydivestmentsandtheoutrighteliminationofproxyvotingbybanks.

Thecompromiseoverbankpowerreachedinparliamentarynegotiationscalledforbanks tomakeachoicebetweenvotingtheirownsharesinacorporationandvotingtheproxiesof depositedshareswherebanksstakesexceeded5%ofthefirm'sequity.Followingthese concessionsinthepoliticalbargaining,thebanksandtheBDBfellsurprisinglysilent.[37] Given theanti-banksentimentthathaddrivencorporategovernancereformontothepoliticalagenda,it appearsthattheBDBandtheindividualbankssawthebenefitsofkeepingalowprofileinthe ongoingdebate.TheBDBdidnotevenofferanystrongopinionsonthecompromisethatwould dilutethebanks'votingpower.Itappearsthatthemajorbankswerelargelyinagreementwith theagendaofcorporategovernancereforminordertoimproveanddeepenGermansecurities markets.[38] Theyhadalreadytargetedfinancialservicesandtheconsultingbusinessgeneratedby thesemarketsastheirgrowthareaandhadreconsideredtheirtraditionalroleincorporate governance.Likewise,theyaccededtomodestlimitationsplacedonthenumberofboard mandatesthatcouldbeheldbyoneperson.Inthebanks'view,largenumbersofinterlocking boardmandateshadgeneratedincreasinglybadpublicitywithoutcontributingtotheir profitability.Withthemostcontroversialitemsremovedfromtheagenda,theattackonbank powerfadedastheissuesoffinancialtransparency,theroleoftheboard,andtheuseofnew mechanismsoffinancingandcompensationemergedasthecoreconcernsofthereforms.

TheCDUandFDPproposedanumberofadditionaltermsthatsparkedfurther controversy.Onewasalimitonthemaximumsizeofsupervisoryboards.Asecondwasan FDPattempttobaroratleastlimitcross-shareholdingamongcorporations.Bothofthese initiativeswereblockedinshortorder.AllianzandMunichRe,theGermaninsurancegiants,in particularfoughtagainstanymandatoryabolitionoftheirlargeandextensivecross-

[36] Moreover,itisnotclearthattheSPDwasinterestedinpushingthedivestitureprovision.Thepubliclyowned Landesbankenownalargeamountofcorporatestock,generallyinsmallerbutlocallyimportantfirms.ManySPD politicianswerenoteagertoseealawthatbrokethetightfinanciallinkagesthatensuredstablecreditandfinancing tofirmsintheirjurisdictions.

[37] Interviews,MarkusHerdina,DAI,Frankfurt,December6,1999;HelmutAchatz,DAI,Frankfurt,December6, 1999;MarcusBecker-Melching,BDB,Berlin,November11,1999;Dr.RainerFunke,MemberoftheBundestag, FDPBundesfraktion,Berlin,November2,1999.

[38] Interviews,MarkusHerdina,DAI,Frankfurt,December6,1999;HelmutAchatz,DAI,Frankfurt,December6, 1999.ArepresentativeoftheBDBalsosuggestedthatthiswasgenerallythecase,thoughwithreservationsonthe particularsofthereforms.Interview,MarcusBecker-Melching,BDB,Berlin,November11,1999.

shareholdings. Compulsory divestment, as in the case of bank equity stakes, would force the insurers and a large number of other firms to incur huge capital gains tax liabilities. The CDU and FDP saw that the provision was likely to trigger potent opposition throughout corporate Germany and quickly dropped it.[39]

The proposed limitation on the size of the supervisory board entangled the legislation in the politics of codetermination. The limit was ostensibly justified as a way to ease the inevitable collective action problems of coordinating the activities of a large number of people. A smaller board would be more cohesive and effective. However, diminishing the size of the board would reduce or eliminate the board seats granted to the unions. Under the Codetermination Act of 1976, firms with more than 2,000 employees received equal representation on the supervisory board. A number of these employee seats had been reserved for the unions that represented employees in these firms. While the proportion of employee representative seats would have remained stable, the number of employee seats as a whole would have to be cut. Because the legislation would have left mandatory representation for blue-collar, white-collar, and managerial employees intact, the reductions would have fallen disproportionately on union representatives who have taken board seats as a matter of established practice, not as a legal requirement.[40] The unions and the SPD therefore justifiably saw this proposal as an attack on codetermination and organized labor. The heads of the DGB (the umbrella association of the industrial unions) and the more conservative white-collar union association went to the Economic Ministry to protest the proposal. Further, the reduction of board size would leave the representatives of *managerial* employees with a stronger position. Because this outcome would strengthen management in corporate governance advocates of shareholder value did not support the board size reduction proposal. Thus, the array of interest groups and policy makers advocating shareholder value policies retreated from a divisive political and economic fight over the role of labor in firm governance and focused on more important issues in the reform of company law. Faced with the prospect of intense opposition from both the left-wing and

---

[39] Interviews, Dr. Rainer Funke, Member of the Bundestag, FDP Bundesfraktion, Berlin, November 2, 1999; Dr. Ulrich Seibert, Leiter des Referats für Gesellschaftsrecht und Unternehmensverfassung, Ministry of Justice, Berlin, July 5, 1999 and November 11, 1999.

[40] Thus, the unions would be caught in a dilemma: either they lost their board seats or they fought to keep their seats and risked alienating their rank and file employees. Interview, Dr. Roland Köstler, Deutscher Gewerkschaftsbund (DGB - the German Federation of Trade Unions) and Hans Böckler Stiftung, Düsseldorf, December 12, 1999.

centrist unions on an issue of great symbolic importance but relatively little practical value, the CDU quickly retreated and dropped the provision from the draft law.[41]

The political constraints created by codetermination also precluded any serious consideration of adopting shareholder primacy as the basis for directors' fiduciary duties. Under codetermination, German company law expressly recognizes and protects the interests of multiple constituencies. As a result, directors' duties are conceived as requiring them to act in the best interests of the "enterprise," rather than those of the shareholders as is generally the case under American law.[42] Consistent with employee representation and the stakeholder model, company law does not privilege shareholder interests. Directors owe fiduciary obligations to the *corporation as a whole*, to employees no less than shareholders. Any attempt to impose a hierarchy of legal interests and norms would have eroded the practical effect of employee representation and would have been seen as an assault on the institution of board codetermination. Thus, a legal norm of shareholder primacy was regarded as politically impossible and not worth considering by those inside and outside the political system.[43]

C. Final Form: The Control and Transparency Act (KonTraG)

The final product of the negotiations was drafted in the Ministry of Justice and entitled the Control and Transparency Act (Kontrol und Transparenz Gesetz), or KonTraG. Because company law is an exclusive concern of the federal government, the Bundestag alone determined the substance of company law. Neither the Länder (states) nor the Bundesrat[44] played any appreciable role in the process. Also in contrast to the American legislative process, the drafting of legislation in Germany is centralized in one government ministry and under the control a single responsible official.[45] As the primary drafter of the KonTraG, Dr. Ulrich Seibert, a senior

---

[41] Interviews, Dr. Rainer Funke, Member of the Bundestag, FDP Bundesfraktion, Berlin, November 2, 1999; Dr. Ulrich Seibert, Leiter des Referats für Gesellschaftsrecht und Unternehmensverfassung, Ministry of Justice, Berlin, July 5, 1999; November 11, 1999.

[42] However, many American states have enacted statutes allowing corporate directors and officers to consider the interests of non-shareholder constituencies such as employees, suppliers, customers, and local communities in responding to a hostile takeover bid. The case law in the United States, including the decisions of the Delaware courts, is frequently ambiguous and inconsistent with respect to the recognition of non-shareholder interests by corporate fiduciaries in the takeover context. *See* Cioff, 2002, Chap. 6.

[43] Interview, Dr. Rainer Funke, Member of the Bundestag, FDP Bundesfraktion, Berlin, November 2, 1999.

[44] The Bundesrat forms the upper house of the German parliament where Länder representatives must approve legislation implicating Land jurisdiction or interests.

[45] In the United States, the drafting of major pieces of legislation is dispersed among multiple congressional committees, subcommittees, and individual members, and their respective staffs. This fragmented structure makes authorship much harder to determine and diminishes the technical and conceptual consistency, clarity, and coherence of legislation. On the other hand, the German system of professionalized legislative drafting tends to

civilservantintheMinistryofJustice,hadsubstantialinfluenceoverthespecifictermsand technicaldetailsoftheprovisions.Ho wever,thesubstanceofthelawwasdeterminedbythe politicalbargainingintheBundestag.

DespitethefactthattheKonTraGwasGermany'sfirstsignificantcompanylawrevision sincecomprehensiveoverhauloftheAktiengesetzin1965,thefinalreform swerefairlymodest inscope.Forpoliticalreasons,theysteeredclearofthecoreconceptsandstructuralfeaturesof Germancompanylawandcorporategovernance.Thoughnotnearlysoextensiveasthe1965 revision,theKonTraGdoesinstituteanumber ofsignificantchangesincompanylawand, perhapsmoresignificantly,embracesanumberofAnglo -Americanconceptionsandpractices importedfromtheincreasinglyinternationalcorporategovernancedebate.Abriefsummaryof thelaw'sprovisionsfollows .[46]

BankPowerandOwnership

Asdiscussedabove,thelawsoughttotrimtheinfluenceofGermany'spowerful universalbanksbyforcingthemtomakeachoice:iftheirholdingsexceed5%ofacorporation's stock,theycanvotetheirownequitystakes *or*vote theproxyvotesofthesharesdepositedby theirbrokeragecustomers. [47]Banksmustalsodiscloseallotherboardmandatesheldbytheir representativesandtheirownershipstakesinfirms.Theseprovisionsweretheremnantsofthe SPD'smobilizationofp opulistoutcryagainstbankpowerthathadbeeninstrumentalinplacing companylawreformonthepoliticalagenda.Inaddition,theKonTraGrequiresbankstoinform theirsharedepositorsofalternativewaystoexercisetheirvotesandstrengthenstheir statutory fiduciaryobligationtovoteproxiesinthebestinterestsoftheaverageshareholder.Banksvoting depositors'proxyvotesmustalsonameamanagementboardmemberasresponsiblefor monitoringthevotingofproxies. [48]TheseprovisionssoughttoutilizeandstrengthentheGerman bank-basedsystemofproxyvoting,ratherthanundermineit,whilecreatingopportunitiesfor alternativemechanismsofproxyvotingtoemerge(suchasshareholders'associations).Inits finalform,theKonTraGdidnot threatencriticalbankinterests.The5%ruledidcreatean

---

concentratesubstantialpowerinthehands ofcivilservantswhooftenwieldconsiderableinfluenceoverthefinal termsofthelaw.

[46]AthoroughandusefulsummaryoftheKonTraG'sprovisionsisprovidedbythelaw'sprincipaldrafter,Ulrich Seibert(1999).

[47]TheActalsoformallyrecognizest heprimarydutyofcustodianbanksinvotingproxiestoprotecttheinterestsof theshareholder,thusimportingaversionofshareholderprimacyintothenormativeframeworkofcorporate governance.

[48] *See* StockCorporationAct (AktG),§128(2).

incentiveforbankstoreducetheirequitystakesincorporations,butasteadyliquidationofthese holdingswasalreadypartofthebanks' planstomodernizetheiroperationsanddevelopinto globalinvestmentbanksandfinancialservicescompanies.Thus,thisreformwaslargelyapiece ofsymboliclegislationratherthanasignificantstructuralreformofthepost -warbank -centered financialsystem.

Auditing,Transparency,andtheRoleof theSupervisoryBoard

TheKonTraGshiftsinformation —andpower —tothesupervisoryboardbyrequiringthat theexternalauditorbehiredby,andreportto,thesupervisoryboardinsteadofmanagement board.[49]Thisprovisionsoughttoredressthemassiveimb alanceofinformationandpower favoringthemanagementboardandtopromoteinternaltransparencyofcorporatefinances.The annualauditmustalsonowincludeanassessmentofriskmanagementandmonitoringsystems.[50] Thelawcontainsadditionalauditingreforms(ofparticularinterestinthewakeoftheEnron scandalintheUnitedStates)toimprovethetransparencyofcorporatefinancesbyensuringthe independence,reliability,andaccountabilityofauditors:

- Anauditorisprecludedfromauditinga firmifithasearnedmorethan30% ofits revenuesfromtheclientoverthepastfiveyears.
- Theauditormustrotatethesignatoryoftheauditifthesamepersonhassigned thereportmorethansixtimesintenyears.
- Thelimitationonauditorliabil itywasraisedfrom500,000DMto8millionDM forlistedcorporations(2millionDMforunlistedcompanies).

TheKonTraGalsomarginallystrengthedtheindependenceandactivismofthe supervisoryboardbyreducingthemaximumnumberofsupervisoryboa rdmandatesfromten perpersonbycountingthesupervisoryboardchairastwopositions.Thelawrequiresthe disclosureoftheotherboardmandatesheldbynomineestothesupervisoryboardtotheAGM andregularreportingofboardmandatesheldbymemb ersofboththemanagementand supervisoryboardsothatshareholderscandiscernpotentialconflictsofinterest.TheKonTraG alsoraisestheminimumnumberofboardmeetingsinlistedfirmsfromtwotofourperyear.

TheOneShare -OneVotePrinciplea ndCross -Shareholding

Asecondimportantprovisionprotectedandempoweredminorityshareholdersby prohibitingunequalvotingrightsamongsharesofcommonstockandthereforeimposeda"one

[49] StockC orporationAct (AktG) ,§§170.1,171.1(supersedingCommercialCode,§318.1).

share, one vote rule" for the first time in Germany. This provision instituted shareholder democracy as a general principle of company law that weakens the control of insiders, and benefits smaller shareholders by ensuring that the degree of a shareholder's control over a corporation would be equal to the amount of capital at risk. Accordingly, the KonTraG also abolished voting caps that limited the maximum number of votes by one shareholder. These caps had prevented changes in control through the accumulation of shares on the markets, thereby reducing managerial accountability as well as the liquidity and dynamism of the securities markets. The one share-one vote rule simultaneously promised to reduce the control premium that attached to the shares of certain favored insider shareholders (such as founding families of their successor controlling shareholders) and encourage the development of more diffuse shareholding by reducing the rents that insiders could potentially divert to themselves through the exercise of their controlling stakes. In other words, the KonTraG reduced the risks of being a small or dissident shareholder.[51]

In contrast to the general principle of one share-one vote, the KonTraG *prohibits* the voting of cross-shareholding stakes above 25% in supervisory board elections.[52] A firm with an ownership stake of 25% or more may not vote *any* of its shares in board elections. This provision was designed to prevent managers from wresting control from shareholders by engaging in reciprocal voting with the managers of other firms involved in cross-shareholding relationships. However, these provisions would expose German firms to the threat of hostile takeover to an unprecedented degree by depriving them of these traditional defensive ownership structures. Although a number of the backers of the KonTraG saw the increased threat of takeovers as a beneficial mechanism of governance and accountability, this new vulnerability would transform the interests of German interest groups and politicians in an unfolding domestic and European debate and political struggle over takeover regulation that continues to this day.

Stock Repurchases and Stock Option Plans

---

[50] Stock Corporation Act (AktG), §93.1.
[51] However, controlling shareholders, particularly the founders of family controlled firms and their heirs, put the government and Bundestag under intense pressure to preserve their voting rights. These interests portrayed the proposed elimination of existing voting structures and caps as a taking of private property. With the support of major firms and industrial association, the KonTraG contained a compromise grandfather provision that *maintained* existing multiple voting share structures for a five-year grace period and *prospectively* mandated the one share-one vote share voting structures. Seibert, 1999: 72 (discussing abolition of voting caps and limited grandfathering of multiple voting rights).
[52] The 25% figure is significant in that this represents a blocking minority under German company law with respect to important corporate decisions.

The KonTraG incorporated Anglo-American concepts of shareholder value and financial practices by allowing stock repurchases and the use of stock options as executive compensation for the first time. Repurchases would allow the corporation, through its managers and only with the shareholders' approval, to acquire up to 10% of the corporation's own stock in order to increase its market price and the ratios of capital, assets, and/or earnings per share. Share buybacks are governed by norm of equal treatment of shareholders, typically (in the case of listed firms) through open market acquisitions. This would also allow shareholders to capture capital gains rather than immediately taxed dividends and remove the incentive for managers to use retained earnings for inefficient investment projects. The corporation can hold acquired shares in reserve for resale in the future or for use in share deals to effect mergers and acquisitions.[53] Enabling corporations to increase the amount of equity capital for stock options was deliberately structured to align the interests of managers and shareholders along the lines of neo-classical economics and American practice in the 1980s and 1990s. However, in contrast to the controversial American practice of granting large options packages without fixed conditions or performance criteria, the KonTraG requires that the shareholders approve of all option plans, and that the plan set benchmarks for the issuance of options. It also prohibits the repricing of options if the company stock sinks below the price paid per share under the option's terms (the strike price of the option). Having examined the abuses of the American system of executive compensation and working within a more egalitarian political and economic tradition, German policymakers were under pressure from across the political spectrum to ensure that options would not become an efficient method to siphon off the corporate treasury and the shareholder's capital.

Accountability and Litigation Rules

Finally, the KonTraG contains very limited reforms of shareholder litigation rules. These measures balance the utility of litigation and civil liability for breaches of fiduciary duties against the threat of abusive shareholder litigation. Frivolous shareholder litigation is commonly associated with corporate governance and legal practice in the United States but has also increased in Germany. The KonTraG lowered the quorum threshold of minority shareholders required to demand the filing of a claim against supervisory and management board members on

---

[53] Within three months of the passage of the KonTraG, 48 corporations had adopted share buy-back plans, including Metallgesellschaft, SAP, SGL Carbon, BASF, Schering, Möbel Walther, and Hofbrau. *See* Seibert, 1999: 74 & nn. 37-43.

behalf of the corporation for gross breaches of the fiduciary duty of loyalty.[54] This quorum was reduced from a vote of 10% to 5% of shares or 1 million DM of nominal capital. However, the KonTraG did not alter the *substance* of fiduciary duties. Although the law lowered the ownership threshold for those seeking to compel the filing of a lawsuit against directors, the KonTraG did not substantially enhance the mechanisms and procedures of enforcing shareholder rights against the management and supervisory boards to make them more effective or prevalent in practice. German law still has no true equivalent of the derivative suit, the class action, or even the contingency fee for attorneys that have made litigation an effective—but also frequently abused—corporate governance enforcement mechanism in the United States.

IV. The New Legal Infrastructure: Company Law, Financial Market Reform, and Labor Relations

The KonTraG was quite deliberately constructed to introduce an element of neo-liberal corporate governance into a traditionally bank-centered neo-corporatist regime. In this the legislation was consistent with the securities law reforms that had transformed the terrain of German, and European, financial market law during the 1990s. Indeed, the KonTraG was designed to support policy goals of the Financial Promotion Laws[55] and the government's

---

[54] Such lawsuits are similar to derivative suits under American corporate law, with the significant difference that the minority shareholders and their counsel do not control the litigation as in the United States. Also, this reform did not extend to claims for breach of the fiduciary duty of care (*i.e.*, some level of sanctionable negligence in carrying out directorial responsibilities) for fear of creating excessive litigation and risk aversion by managers and supervisory board members.

[55] *See* Securities Trading Act (Wertpapierhandelsgesetz-WpHG) of July 26, 1994, §§3-11 (Federal Law Gazette, Part I, p. 1749), promulgated as Article I of the Second Financial Promotion Act (Gesetz über den Wertpapierhandel und zur Änderung börsenrechtlicher und wertpapierrechtlicher Vorschriften, Zweites Finanzmarktördnungsgesetz) (enabling legislation for the creation of the BAWe); Amendment to the Securities Trading Act by Article 3 of the Third Financial Market Promotion Act (Gesetz zur weiteren Fortentwicklung des Finanzplatzes Deutschland, Drittes Finanzmarktförderungsgesetz) of 24 March 1998 (Federal Law Gazette Part I p. 529).

For additional statutory reforms of the German securities markets and securities regulation in the remarkable overhaul of the financial system in the late 1990s, *see* Prospectus Act (Verkaufsprospektgesetz) as announced on 9 September 1998, Federal Law Gazette, Part I, p. 2701, as last amended by Article 2 of the Act on the Further Promotion of Germany as a Financial Centre (Third Financial Market Promotion Act) of 24 March 1998 (Federal Law Gazette I p. 529); Amendment of the Securities Trading Act (Wertpapierhandelsgesetz) by Article 2 of the Law Implementing the EC Deposit Guarantee Directive and Investor Compensation Directive of 16 July 1998 (Federal Law Gazette I, p. 1842); Amendment to the Securities Trading Act by Article 2 of the Law Implementing EC Directives for the Harmonisation of Regulatory Provisions in the Field of Banking and Securities Supervision (Gesetz zur Umsetzung von EG-Richtlinien zur Harmonisierung bank-und wertpapieraufsichtsrechtlicher Vorschriften) of 22 October 1997 (Federal Law Gazette Part I p. 2518); Amendment to the Securities Trading Act by Article 16 of the Judiciary Notification Act and the Act Amending Cost Law Provisions and other Laws (Justizmitteilungsgesetz und Gesetz zur Änderung kostenrechtlicher Vorschriften und anderer Gesetze, JuMiG) of 18 June 1997 (Federal Law Gazette Part I p. 1430) (entered into force 1 June 1998).

sustainedpolicyinitiativesseekingtoestablishashareholdercultureinGermany.[56]The FinancialPromotionLawshadcreatedoneleveloflegalinfrastructure,includingGermany's firstfederalsecuritiesregulator(theBAWe)forthedevelopmentofsecuritizedfinance,the spreadofshareholding,andthediffusionofcorporateownership.Theadoptionofdisclosure rulesandthecreationofaregulatoryagencychargedwithrulemakingandenforcementinthe realmofsecuritiestradingrepresentedaconvergenceontheAmericanSECmodelofsecurities regulation.TheKonTraGsharedthefundamentalnormativecommitmentsofthenew frameworkofsecuritieslawtotransparency,equaltreatmentofshareholders,andcurbingthe rentseekingofcorporateinsiders.Thelaw'sprovisionsincreasingtheindependence,autonomy, andactivismofthesupervisoryboardtrackedthecorporategovernancedebateasithademerged intheAnglo-Americaneconomiessincethe1980s.Likewise,itsprovisionforgreaterflexibility infinancingandincentive-basedcompensation drewfromthegovernancetheoriesofneo-classicaleconomicsandAmericanfinancialandmanagementpracticesthatexercised considerableallureoverseasduringthedecade.[57]Inshort,whereastheFinancialPromotion Lawsimprovedtransparencyandaccountabilityatthelevelofthemarkets,theKonTraGwas intendedtodothesameatthelevelofthefirm.Thisrelationshipbetweensecuritiesregulation andcompanylawpointstotwolevelsofinfrastructurenecessaryforthetypeofsecuritized financethat definesamodernfinancialsystem.Onelevelisexternaltothefirm,theother internal,andtheymustcomplementandreinforceoneanother.

ThepolicymakersandinterestgroupsthatnegotiatedtheKonTraGbelieveditwasa necessaryintermediatestepinabroaderstructuralreformoftheGermaneconomy.Itwas necessary,butnotsufficient.ThereformofcompanylawwasnecessaryfortheGerman corporationtobecomeavehicleforandrecipientoftheequityfinancethattheFinancial PromotionLaws wereintendedtomakeavailable.Yet,eveninconcertwiththeFinancial PromotionLaws,theKonTraGcouldnottransformthetanglednetworkofownershipthat insulatedcorporateGermanyfromthedemandsofthefinancialmarketsandshareholders. Therefore,theprojectoffinancialmodernizationandeconomic(*i.e.*,corporate)restructuring

---

[56] *See*Ziegler,2000:206-208(discussingtheprivatizationandflotationofDeutscheTelekomshares,theeffortsof theResearchMinistrytojump-startamarketforventurecapital,andthepublic-privateeffortspurringthe developmentofthetechnology-intensiveNeueMarktequitymarketinFrankfurt).
[57]ManyobserversinEuropebelievethatthealurewasespeciallypowerfultoGermanexecutiveswhoenviedthe compensationpackagesoftheirAmericancounterparts.Toparaphraseoneinterviewee,thefondestwishofGerman executivesistobeprotectedbyGermancompanylawbutpaidlikeanAmerican CEO.

begununderthe CDUcoalition(inpartthroughinstigationbytheSPD)requiredfurther structuralreformsofthestructureofcorporateownership.TheSPDpursuedth isagendawhenit tookcontrolofthegovernmentunderGerhardSchröder.Itenactedthemostsweepingtax reformlegislationinpost -warGermanhistoryinordertounwindthewebofcross shareholdings thatheld“GermanyInc.”inplace.Insum,allthree setsofreforms(securitiesmarket,company law,andtaxation)werenecessarybeforegenuineandeffectivecorporategovernanceand financialsystemreformcouldbecomepossible. [58]

Thesereforms,however,leftmuchofthecoreofcompanylaw’snormative framework wasleftuntouched.ThesubstanceoftheKonTraGrevealstheoppositionalforcesworking withintheGermanpoliticaleconomyasitselitessoughttoaccommodatetheGermanmodeltoa neweraoffinanceandcorporateorganization.Neithercodete rmination,northesubstantive contentoffiduciarydutieswerealteredwithrespecttointra -firmrelations. [59]Fiduciaryduties werestrengthenedonlyastheyrelatedtoexternalrelationsinthefinancialservicesindustry. Banksnowoweastricterduty ofloyaltytotheircustomers.Insidethecorporation,directors’ fiduciaryobligationsremainessentiallyunchanged.Astheyapproachedthesubjectofcompany lawreform,politiciansknewthatitwouldbeimpossibletoinstitutealegalnormofshareho lder primacyoranyarticulationoffiduciarydutiesthatcompromisedcodeterminationwaspolitically impossible.Suchanormwouldleadtooneoftwopoliticallyunacceptableresults.One possibilitywouldbethehollowingoutofsupervisoryboardcodet erminationbyimposingon employeerepresentativesafiduciarydutytoactinthebestinterestsofshareholders,ratherthan theiremployeeconstituents.Thiswouldeffectivelyrepealcodeterminationandleaveitan emptyinstitutionalshell.

Asecond possibilitywouldhavebeentodefinetheobligationsofsupervisoryboard directors’intermsoftheirrespectiveconstituency(*i.e.*,shareholders,bluecollaremployees, whitecollaremployees,andseniormanagement).Shareholderrepresentativeswouldo we stringentdutiestoshareholders,andemployeerepresentativeswouldhavecompletelydifferent

[58]Pensionreformconstitutesthefinalcomponentofthetransformationof Germanfinanceandcorporate governance.Thisprocessisonlynowbeginningwithamodestsetofreformsencouragingtheformationofprivate pensions.Themostsubstantialpo liticalbattleshaveyettobefoughtoverthefundingofcorporatepensions:the dominantformofprivatepensions(individual,company -level,orsectoral),theidentityoftheirmanagement (insurancecompanies,banks,mutualfunds,and/orpensionfunds), andtheirformofgovernance(professional moneymanagement,managerialdomination,orcodeterminedboardsoftrustees).

[59]TheGermancourtshaveinferredtheexistenceofandelaborateduponfiduciarydutiestoshareholders,butlaw remainsundeveloped andconceptionsofcorporateinterestdistinctfromshareholderinterestpersist.

obligations.Althoughlogicallypossible,thissolutiontotheproblemoffiduciarydutiesunder codeterminationposesbothpracticalandtheoreticalproblems.Asapracticalmatter,this divisionofdutieswouldunderminecodeterminationinlargecorporations.Codeterminationis intendedtoproduceconsensualnegotiationsanddecision-making,whereasdivergentfiduciary dutieswouldcompeltheopposingblocksofdirectorstovoteagainstoneanotheronimportant andcontentiousissues.Theoretically,fiduciarydutiesareconceivedasaunifiedcoherent whole.[60]ItisabedrockprincipleofGermancompanylawthattheseobligationsareowednotto shareholdersoranyotherparticularisticconstituencybuttotheenterpriseitselfasanongoing entity.Thiscorporatistconceptionofobligationcomplementstheinstitutionalstructureof codetermination,butdoesnotsupportthenormofshareholderprimacyordichotomous conceptionsoffiduciaryduties.

Theproblemoffashioninganefficaciousdefinitionoffiduciarydutiesthatcouldguide theconductofintra-corporateaffairsandprovideameansofadjudicatingcorporatedisputes indicatesthepersistentinfluenceofcodeterminationonthedevelopmentofcompanylaw. Codetermination—andlaborpoliticsgenerally—imposesubstantialconstraintsonthe developmentofanythingapproximatingAnglo-Americanshareholdercapitalism.Asidefrom theissuessurroundingfiduciaryobligations,theabandonmentoftheproposedreductioninthe sizeofthesupervisoryboardprovidedtheclearestexampleofthepowerofthisconstraint.The reductionofsupervisoryboardsizewassupportedbybusinessandfinancialinterests,aswellas byeconomictheory,butwaskilledbyunions(withjustification)onthegroundsthatit constitutedanindirectattackontheirroleincodeterminationandcorporategovernance. Moreover,ascodeterminationisastructuralremedytotheproblemofemployeerepresentation, itprecludesalternativestructuralarrangementsdesignedtoenhanceshareholderinterestsand maximizeshareholdervalue.Constraintsimposedbycourtsonuseofboardcommittees comprisedsolelyofshareholderrepresentatives(*i.e.*,outsidedirectors)donotallowtheboardto focusontheinterestsofdifferentconstituenciesindifferentcontextsbyrestructuringitselfinto specializedunits.

---

[60]However,theCodeterminationCaseof1979,inwhichtheFederalConstitutionalCourtupheldthe constitutionalityoftheCodeterminationActof1976,recognizes—atleastimplicitly—thedifferinginterestsof employeesandshareholders,andthusoftheirboardrepresentatives.TheCourtheldthattheCodeterminationAct wasnotatakingofshareholderpropertyoranabridgementofthebasicrightoffreeenterprisebecause shareholders retainthetie-breakingvoteofthechairofthesupervisoryboardandthereforeremainindefactoandlegalcontrolof thecorporation.

Given these impediments to fundamental reform of the supervisory board and fiduciary duties necessary for convergence on the American model, reform of the German stakeholder system strongly favors increased transparency. Theoretically, codetermination should discourage legal reforms that would mandate greater disclosure and transparency within the firm. Increased information flow to the supervisory board would strengthen both shareholders and employee representatives (and the unions). The KonTraG provides ambiguous evidence on this point. On the one hand, the law did significantly improve internal corporate transparency by increasing the supervisory board's control over auditing and thus monitoring of management. On the other hand, the KonTraG linked this intra-firm transparency to audit functions that have been closely related to public financial reporting. This raises the possibility that the increased information flow to the board will not exceed that going into public disclosure and suffer from the familiar problems of opaque and distorted accounting. However, the basic shift in power and control effected by the KonTraG in favor of the supervisory board in auditing matters puts that body in a far stronger position to question auditors and managers about the firm's finances. This suggests that codetermination has not constrained the development of internal transparency, monitoring, and accountability mechanisms to a significant degree.[61]

The preclusion of shareholder primacy as a legal norm in a codetermined governance system and distaste for litigious enforcement mechanism has prevented fiduciary law from developing along liberal lines. With the exception of the fiduciary relation between banks acting as securities brokers and their customers depositing shares, no articulations of fiduciary duties and shareholder primacy were made for fear of contradicting the norms and institutionalization of consensual governance represented by codetermination that require equal concern and consideration of shareholder and labor interests. A recent landmark decision by the Federal Supreme Court strengthened the fiduciary obligations of supervisory board members to defend the interests of shareholders against managing board members yet it could not endorse shareholder interests over those of employees.

[61] The caveat must be added: the board may not use these new powers under the KonTraG for fear that labor will appropriate the gains from internal transparency, or a sufficiently large portion thereof that would render the effort and expense of monitoring futile. This empirical question can only be answered through additional detailed research at the firm level.

Likewise, the KonTraG largely eschewed litigious mechanisms of governance and enforcement in favor of structural fixes.[62] The minimal changes in the formal rights of shareholders and duties of directors contained in the KonTraG, and the law's modest liberalization of litigation rules regarding suits against directors are peripheral matters compared to the provisions reforming the powers and role of the board. There are two principal reasons for this preference for structural reforms inside the governance structure of the firm. First, formal and enforceable rights give rise to a functional and predictable order of governance relations only where these rights describe and impose a hierarchical order of legal entitlements. In American law, this hierarchy is clearly fashioned by the norm of shareholder primacy and a corporate structure that provides no mechanism for employee representation. Codetermination creates an institutional structure and a corresponding normative understanding of corporate governance that legitimates multiple interests. As a result, *adjudication* of conflicts among these interests becomes exceedingly difficult, if not impossible. Conflicts must be *negotiated* internally within the firm rather than adjudicated externally in a court. In strengthening the board, the KonTraG inevitably strengthened both shareholders and employees. In a codetermined structure of representation, transparency favors both constituencies against managers and controlling shareholders.

Second, policymakers had sufficient experience with "predatory" lawsuits in Germany and enough information about the securities litigation industry in the United States to dissuade them from creating litigious mechanisms of corporate governance. Germany traditionally has had weak securities laws and procedural mechanisms that discouraged litigation. However, German company law contains a quirk that has created Germany's own version of the litigation industry. The conduct of the annual general meeting of shareholders (the AGM) under German company law is subject to complex procedural rules and a failure to comply with them can provide the basis for an action to rescind a corporate decision and enjoin its execution. As a result, an active plaintiffs' bar has developed to challenge important corporate decisions requiring shareholder approval on procedural grounds. These lawsuits are frequently without merit, but nonetheless threaten to delay critical corporate transactions and plans. Thus, just as in the case of many American securities suits, German company law actions are frequently brought

[62] And even these structural remedies to governance problems of insider opportunism and managerial accountability were limited by codetermination as demonstrated by the debate over supervisory board size.

not because of their merit, but because of the leverage they exert on management to extract quick, but lucrative, settlements. Because German law provides for easier access to the courts in cases arising out the conduct of the AGM than in the trading of securities, lawsuits are frequently filed to enjoin the execution of important business decisions where time is of the essence (such as in the case of an urgent capital increase or corporate acquisition) where the leverage of the plaintiff's attorney is maximized. Those who negotiated and drafted the KonTraG had no interest in expanding the opportunities for a type of legal practice they viewed as wasteful, extortionate, ineffective in the achievement of policy goals, and disruptive to the patterns of cooperation and negotiation favored and maintained by neo-corporatist institutional arrangements.

V. Unwinding Germany, Inc.?: The Mannesmann Takeover and Tax Reform

Taken in isolation, the KonTraG reforms appeared modest and unlikely to cause a substantial change in German corporate governance practice and policy. Several conjunctural developments following the passage of the KonTraG, however, threatened the interests of German elites in corporate governance: (1) Vodafone's hostile takeover of Mannesmann, (2) major tax reforms designed to break up German cross-shareholdings, and (3) the negotiation of a EU Takeover Directive. In this context, the KonTraG's elimination of takeover defenses provided by unequal share voting rights, voting caps, and cross-shareholding shifted the policy preferences—and fears—of German elites and the politics of corporate governance reform in Germany. Taken together, German economic and political elites believed that these developments would render domestic corporations asymmetrically vulnerable to takeover by better-protected firms from the United States and other European countries. The KonTraG reforms inadvertently mobilized political and economic elites against further liberalization of company and takeover law.

A. The Mannesmann Takeover

A sign of substantial change in German corporate governance arrived with Vodafone's hostile takeover of Mannesmann.[63] Mannesmann had been an established Düsseldorf-based metalworking and engineering firm, but made an extraordinarily successful transition to wireless telecommunications. The company also found itself suspended between the traditional structures

and practices and German corporate governance and the new rules of shareholder capitalism. Mannesmann had pursued shareholder value avidly. Its high share price financed a series of strategic acquisitions that turned it into one of Europe's leading wireless telecommunications companies and an attractive investment for investors around the world. However, it had not adopted IAS or US-GAAP accounting standards, remained a diversified corporate group (*Konzern*), and it neither listed on either the New York or London stock exchanges nor made return on equity the central criteria for evaluating corporate strategy.[64] By 1999, its stock market capitalization equaled 11.5% of the German blue-chip DAX index. Its shares were widely held, rather than locked up in cross-shareholdings, and foreign investors held 60% of its stock—and Anglo-American investors owned 40% and Anglo-American institutional investors held 19.2%.[65] In November 1999, Vodafone, a smaller British wireless telecommunication corporation more thoroughly adapted to the demands of British and international capital markets, launched a successful cross-border hostile takeover bid for Mannesmann.

For the first time, a successful hostile takeover had been launched against a major German corporation by a foreign firm—and under German law no less. The Mannesmann takeover also revealed the surprising weakness of alleged defense mechanisms built into the German model of capitalism and corporate governance. First, relational finance provided no cover. The major German banks did not rise to the defense of the target company and at least tacitly supported the takeover.[66] Mannesmann was also something of a special case. The universal banks did not have major equity holdings in Mannesmann, the company's stock was unusually widely held for a German corporation, and Anglo-American investors held an unusually large percentage of its shares. This made Mannesmann atypically vulnerable to a tender offer bid. Second, supervisory board codetermination failed to create a block of directors capable of warding off Vodafone's bid. Once the bid was made, there was little the directors

---

[63] Höpner and Jackson (2001) provide an excellent detailed overview and analysis of the Mannesmann takeover and its implications for German corporate governance.
[64] *Id*., p. 25.
[65] *Id*., pp. 25-26 & Table 5.
[66] Interview, Dr. Roland Köstler, Deutscher Gewerkschaftsbund (DGB - the German Federation of Trade Unions) and Hans Böckler Stiftung, former supervisory board member of Mannesmann, AG, Düsseldorf, July 18, 2000; *cf.* Höpner and Jackson, 2001: 44-45.

could do to prevent shareholders from tendering their shares because German law did not authorize takeover defenses, such as poison pills, common in the United States.[67]

Notwithstanding the unprecedented nature of the Vodafone tender offer, the political and public response to the takeover bid was surprisingly muted. Chancellor Schröder issued a few critical comments regarding the incursion of Anglo-American capitalism into the Germany, but he was roundly criticized in many quarters —particularly in the business and foreign press —for interfering in a market transaction and he quickly withdrew from an active role in the matter.[68] Although Mannesmann's management fought bitterly against the takeover, it did not want the government's help to drive off Vodafone and sought to conduct its defense through available legal mechanisms and through lobbying shareholders.[69] There was little of the widespread public outcry or union militancy that accompanied the abortive Thyssen Krupp hostile takeover two years before or the near collapse of the Holzmann construction group.[70] Employee representatives on the supervisory board were primarily concerned with protecting the economic interests and job security of their constituents, not with the independence of the firm as an ongoing enterprise. Though IG Metall opposed the takeover, it did not call for mass demonstrations against it.[71] Moreover, CalPERS sided with Mannesmann's management and IG Metall *against* the takeover on the ground that Vodafone's anticipated debt levels and business strategy posed long-term risks to shareholders (concerns later proved correct after the crash of the telecommunications stocks in late-2000 and 2001). The CalPERS criticisms of the takeover blunted potential criticism of the power and influence of the foreign investors and investment funds that owned a substantial percentage of Mannesmann's stock.

---

[67] Indeed, in some important ways German law was more favorable to the hostile bidder than British law. German law allows the bidder to raise the price bid in a tender offer. The law in the United Kingdom, where Vodafone was based and incorporated, prohibited changing the terms of the bid once launched. Vodafone's managers and strategists took advantage of German law by successively raising the bid price for Mannesmann shares, and certainly did not consider the legal defenses available under German company law insurmountable. Interview, Dr. Roland Köstler, Deutscher Gewerkschaftsbund (DGB - the German Federation of Trade Unions) and Hans Böckler Stiftung, former supervisory board member of Mannesmann, AG, Düsseldorf, July 18, 2000; *cf.* Höpner and Jackson, 2001: 44-45.

[68] In fact, his half-hearted and unsuccessful intercession was seen as end of Germany, Inc. and beginning of era of takeovers and restructuring. Takeovers remained unpopular with the public, but opponents of takeovers and economic liberalization failed to mobilize politically around the issue.

[69] For an account of the takeover battle, *see* Höpner and Jackson, 2001.

[70] *Cf.* Ziegler, 2000 (discussing, *inter alia*, the Thyssen Krupp takeover attempt and eventual merger)

[71] Interview, Dr. Roland Köstler, Deutscher Gewerkschaftsbund (DGB - the German Federation of Trade Unions) and Hans Böckler Stiftung, former supervisory board member of Mannesmann, AG, Düsseldorf, July 18, 2000

The public perception shifted, however, as it became clear that the Vodafone-Mannesmann deal was not the merger of equals as had been advertised. Mannesmann had been taken over by a British firm and the German operations were no longer directed from Düsseldorf. This represented something of a blow to German pride, a more serious blow to the economic heartland around Düsseldorf, and a looming threat to Germany's corporate elite. No great economic benefit was seen in the takeover —certainly no benefit to Germany —and an innovative company that appeared to play by the new marketplace rules of shareholder value, high-tech innovation, and widely-held stock was seen as paying the price of its own existence for an economic order driven by speculative financial practices. These perceptions, along with suspicions of shareholder capitalism and its implications for German society and economic sovereignty, permeated the political elite as well.[72] This resentment and fear festered in Germany even though *no* hostile takeovers occurred in Germany in the aftermath of the Mannesmann takeover.

B. Tax Reform and the Unwinding of Cross-Shareholdings

A web of cross-shareholdings traditionally provided the cement that kept "Germany Inc." intact and made takeovers difficult to execute.[73] These cross-shareholding arrangements, however, have been extremely resilient. Firms and financial institutions have refused to liquidate their stakes in other corporations so long as capital gains taxes were prohibitively high (over 50%). In light of these ownership networks, the rather modest reforms brought about by the KonTraG appeared to have little chance of affecting the practice or future politics of corporate governance in Germany. However, Vodafone's hostile takeover of Mannesmann in late 2000 showed the German elites and electorate that the country's firms were now exposed to tender offers from outside the country. Just a few months before, tax reform legislation had removed the structural impediments to unwinding protective cross-shareholdings and would ultimately increase this vulnerability.

[72] Though the extent and intensity of anti-takeover attitudes among political elites is hard to determine without survey data, the shifting government policy on takeover law strongly indicates a substantial turn against neo-liberal corporate governance policies.
[73] *Cf.* Jenkinson and Ljungqvist, 1999; Köke, 2000. These empirical studies found a more active market for control in Germany than commonly thought. Changes in control are made through the sale of control blocks, often with the assistance of banks. They also found, however, that the chances of a change in control and ultimate ownership is reduced by complex ownership structures (*i.e.*, extensive cross-shareholdings). This finding raises the paradoxical possibility that in Germany, concentration of ownership facilitates takeovers while fragmentation of ownership my inhibit them.

ThemajortaxreformlawofJuly2000(*Steuerreform*) *abolished*capitalgainstax eson theliquidationofcross -shareholdings.TheSchrödergovernmentmadeadeliberatepolicy choicetoinvigorateGermansecuritiesmarketsbyincreasingtheproportionofsharestraded(the freefloatofissuedsecurities)andtoinducetheunwindingo fownershipstructuresthatshielded Germancorporationsfrompressurestorestructureandadjusttochangingeconomicconditions. PassedinJuly2000,despitetheevidencethatGermany'sfirmswereincreasinglyvulnerableto takeover,thistaxreformlaw promisestobethemostimportantandradicalcorporategovernance reforminGermanhistory. [74]Thelegislationwasanimatedentirelybycorporatefinanceand governanceconcerns.Theanticipatedeffectsofthelawweretaxneutral.Intheabsenceofthe reductionincapitalgainstaxes,firmsandfinancialinstitutionswouldsimplyhaveleftthecross - shareholdingsinplace.Noadditionaltaxrevenueswouldhavebeengeneratedunderthestatus quoante.Conversely,theeliminationofcapitalgainstaxe sondivestmentswouldnotdeprive thegovernmentofrevenuesthatwouldhavebeenotherwisegenerated.

Oneofthemoststrikingaspectsofthisdramaticpolicyshiftisthatitwaspushedthrough aresistantlegislativesystembyaSocialDemocraticgover nmentwithbusinesssupportover conservativeopposition.BeginningwiththeKonTraGin1998,thepoliticsofcorporate governancehasbeenappropriatedbythecenter -leftcoalitionaspartofanagendaofeconomic andlegalmodernization.Indeed,theta xreformagendabecameacentralpieceoftheShröder government'seconomicmodernizationagendaandrequiredfiercepoliticalmaneuveringtopush thelegislationthroughtheBundesrat,whereCDU -CSUrepresentativesoftheLandgovernments heldthemajorit y.Onlythroughshrewdbargainingandthepromisesofadditionalfederal transferstostrappedLandgovernmentssecuredthelaw'spassage.Economicsdidnotdrivethe reform;politicsdid.

HavingtakeneffectinJanuary2002,thetaxreformlawhasalrea dybeguntosetoffa waveofcorporaterestructuring. [75]Thestrengthoforganizedlaborandcodetermination precludesthesortoftakeoverwavethattheUnitedStatesexperiencedinthe1980s,inwhich employeesborethebruntofadjustmentcosts.Howeve r,forthefirsttimeinGermanhistory,

---

[74] *See*, *e.g.*, Holloway, 2001(interviewwithinternationalcorporategovernanceStephenDavispredicting thatthe 2000taxreformswilltransformGermancorporategovernanceandincreasetakeoveractivity).

[75]However,foreconomicreasonsthisrestructuringisunlikelytobeimmediateandcomprehensive.The underdevelopmentandrelativeilliquidityofGerma ny'scapitalmarketshasconstraineddivestmentofcross - shareholdings. *See*, *e.g.*, Bushrod,2001(b). Inthenearterm,thedispositionofstakeswillprobablyeitherfollow

hostile takeovers became a realistic possibility and this looming threat altered the political terrain of corporate governance reform in Germany. The effects of this shift were felt both within domestic politics and in Brussels as the EU Parliament debated the long-awaited Takeover Directive.

VI. Backlash and the Spillover Effect: The EU Takeover Directive Debacle, the German Takeover Law, and the Limits of the Liberalism

A. The Reconstitution of German Interests and the KonTraG Reconsidered

The KonTraG was not a piece of nationalistic legislation. It was not drafted with an eye towards the defense of incumbent managers or the German model of neo-corporatism nor was it designed to reinforce the social market economy. Even though the political compromises that determined its final form removed those provisions that would most seriously destabilize the German model of corporate governance and political economic arrangements, the law was essentially neo-liberal in its conception and its proponents borrowed heavily from Anglo-American theories and practice in formulating the legislation. The tax reform legislation continued this liberalizing trend and reflected increasing political and economic pressures for the structural reform of established institutional arrangements.

In the context of a liberalized and more shareholder friendly company law, the new tax regime and the Mannesmann takeover increased the salience of the vulnerability of German firms to hostile takeovers. Contrary to numerous predictions in the popular press, the Mannesmann takeover had not been a watershed with respect to hostile takeovers in Germany. No other hostile takeovers by foreign firms occurred following the Vodafone-Mannesmann deal. However, the European Commission's adoption of a draft EU Takeover Directive and its submission to the European Parliament for approval triggered fears of takeover vulnerability among German political and economic elites. With the submission of a proposed EU Takeover Directive to the European Parliament, conflicts over the desirability of hostile takeovers, the strategic advantages conferred by national law, and the interaction of the proposed EU directive and domestic law in reinforcing these advantages proved an explosive combination of political and economic factors. While the KonTraG eliminated anti-takeover defenses and created the legal infrastructure for a more vibrant market for shares, the tax reform law instituted incentives

---

the traditional course of selling blocks of shares (often with a control premium) or proceed incrementally through

tounwindcross -shareholdingsthatprovided *defacto* takeoverprotection. [76]Thisconjunctureof factorsledGermany'spoliticalelitestoopposetheTakeoverDirective.Theresultwasthefirst defeatofamajorEuropeanCommissioninitiativeintheEuropeanParliament.

B. TheEUTakeo verDirective

TheharmonizationofcompanylawhasbeenaprominentitemontheEUagendafor nearlythirtyyears.AcommonEUtakeovercodehadbeeninnegotiationforoveradecade.The firstformalincarnationoftherecentTakeoverDirectiveproposal datesbackto1989. [77]The CommissionpresentedageneralframeworkforthedraftTakeoverDirectivein1996anda furtheramendeddraftversionin1997. [78]The Councilunanimouslyadoptedacommonposition onthedraftDirective inJune2000andCommission acceptedthatcommonposition in July 2000. SenttotheEuropeanParliamentinSeptember2000,theParliamentapprovedthedraft Directive—andfifteenamendments —inDecember2000. TheCommissionandParliament disagreedonanumberofamendmentsdrafted toallowgreatermanageriallatitudeinadopting defensesagainsthostiletakeoversandgreaterconsultationrightsforemployeesofthetarget company.[79]Withlessthanadaytotheexpirationofatreaty -imposeddeadline,theCommission andParliamenta greedtoacommonpositionontheDirectiveonJune6,2001,andformally submittedthedraftDirectivefortherequiredbaremajorityvoteofapprovalbytheEuropean Parliament.Thisvotewouldconstituteawatershedeventineconomicandcorporategove rnance ontheContinent,butitwasnottobethemajoradvancetowardEUpolicymakingandmarket harmonizationenvisionedbyitsbackers.

ThedraftDirectivewastheclearestandmostfar -reachingattempttointroduceAnglo - Americanconceptsofshareholde rvalue,andshareholdercapitalismgenerally,intotheEuropean politicaleconomy.Forthisreason,theDirectivebecameoneofthemostdivisivepiecesof

---

smallerbutslowersell -offsintothesecuritiesmarkets.

[76]Thereformswereexpectedtoincreasethe"freefloat"ofGermanshares(theproportionofafirm'sshares activelytradedonthemarket,asdistinguishedfroms haresheldlong -termbyblockholdersorlocked -upincross - shareholdings).Thiswouldmakecontrollingmajoritiesofsharessusceptibletotenderoffersinamuchlarger numberoffirms.

[77] *See* ThirteenthCouncilDirectiveonCompanyLawConcerningTake overBids,OJC64,14.3.1989,p.8; EuropeanCommission'sAmendedProposal,10September1990,OJC240,26.9.1990,p.7.

[78] SecondProposalforaThirteenthDirectiveonCompanyLawConcerningTakeoverBids,OJC162,6.6.1996,p. 5;ThirdAmendedProposa lforaThirteenthDirectiveonCompanyLawConcerningTakeoverBids,OJC378, 13.12.1997.

[79]ThisindicatesthenovelpoliticsandstructuraldynamicsofeffortstoreformEuropeaneconomies:the counterattackagainstastringentpieceofneo -liberallegi slation,theTakeoverDirective,combinedanembraceof quintessentialAmericananti -takeoverdefensesandanextensionofcodeterminationrights.

legislationtoevercomebeforetheEuropeanParliament,sparkingfierceoppositionandunusual alliances.TheprinciplesarticulatedintheDirectivewouldhavemadetakeoversmucheasier. Byfarthemostcontroversialprovisionandthelightningrodofopposition,Article9ofthedraft imposedarequirementof“neutrality”ondirectorsandsenior managersinrespondingtoa hostiletakeoverbid. [80]Thiswouldhaveprohibitedcorporateboardsandmanagersfromadopting “poisonpills”andotherdefensivemeasureswithoutshareholderapprovalandwouldhave prohibitedthesolicitationofshareholderap provalinadvanceofahostilebid.Thefightover Article9’sneutralitydutieseclipsedtheprovisionsofArticles3and10thatrequiredequal treatmentofallthetargetcorporation’sshareholdersandmandatorybidrulescompellingan offerforallou tstandingsharesofapubliclytradedfirmwhentheacquirer’sholdingsexceededa specifiedlevel.Thecontroversyoverboardneutralityshiftedthepoliticaldebatefromthe improvementofEuropeancorporategovernanceandsecuritiesmarkets,whichthe equal treatmentandmandatorybidrequirementswouldhaveadvanced,tooneovertheeconomicand socialdesirabilityofhostiletakeovers.Furthercomplicatingthecontroversy,thedraftDirective didnotbaralltakeoverdefenses.Itcontainednoone -share,one -voteprinciple,asdoesthe KonTraG,allowedthecontinueduseof“goldenshares”thatconfervotingcontrolover corporationstotheminoritythatholdsthem,andpermitsthesortofprotectivecross - shareholdingthatGermany’staxreformswered esignedtounwind.Thus,theTakeover DirectivethreatenedtorenderGermanfirmsparticularlyvulnerabletotakeoverbycorporations fromcountriesallowinggoldensharesorpoisonpills.Despitetheindicationsofdeep -seated oppositionintheEuropean Parliament,theCouncilrejectedasubstantiveamendmentloosening therestrictionsondefensesandagreedonlytoanextensionofthephase -inperiodforthe provisionfromfouryearstofive.Nonetheless,byJuneof2001themajorityofEUmember

[80]Article9provided:

> Obligationsoftheboardoftheoffereecompany
>
> MemberStatesshallensurethatrules areinforcerequiringthat:
> (a)afterreceivingtheinformationconcerningthebidanduntiltheresultofthebidismadepublic,the boardoftheoffereecompanyshouldabstainfromanyactionwhichmayresultinthefrustrationofthe offer,andnota blyfromtheissuingofshareswhichmayresultinalastingimpedimenttotheofferorto obtaincontrolovertheoffereecompany,unlessithasthepriorauthorizationofthegeneralmeetingof theshareholdersgivenforthispurpose;
> (b)theboardofth eoffereecompanyshalldrawupandmakepublicadocumentsettingoutitsopinion onthebidtogetherwiththereasonsonwhichitisbased.

state governments had approved the draft Directive, as had the European Commission. The political opposition that killed the Directive began in Germany.

C. German Takeover Politics Comes to the European Parliament

The direct and inherent threat posed by takeovers to vested economic interests triggered a shift in German politics against the Takeover Directive. German managers saw the directive as a threat to their own positions and that of German corporations generally.[81] More broadly, the hostile takeover of Mannesmann by Vodafone of the United Kingdom had steeled opposition to takeovers across a broad swath of German interest groups and voters.[82] The German industrial unions, a key pillar of support for the governing SPD, were adamantly opposed to the importation of Anglo-American forms of law, governance, and economic organization. Organized labor saw the Takeover Directive as a means of shifting both power and income from employees to shareholders, as had been the case in the United States and United Kingdom since the 1980s. However, German unions are far more politically and economically powerful than their American, British, and French counterparts. German managers and labor thus formed a potent coalition across class and ideological lines to oppose the Directive.[83]

Opposition to the Takeover Directive was intensified by the sequence of domestic corporate governance reforms in Germany that had the effect of rendering German corporations particularly vulnerable to takeovers under the terms of the Directive.[84] The KonTraG and tax reform legislation together had eliminated the principal defenses to hostile takeovers in Germany. In contrast, the Takeover Directive would have *allowed* both golden shares and cross-shareholding to shield those companies with such ownership structures. This left German firms asymmetrically vulnerable to takeover threats from firms based in France, Italy, and the Netherlands where golden shares are common, and from Italian firms within protective webs of cross-shareholdings and ownership "cascades." Ironically, the draft Directive also would have

---

[81] The managers of DaimlerChrysler, Volkswagen, BASF, and several German chemical companies reportedly led managerial opposition to the Takeover Directive. Volkswagen was a particularly effective lobbyist. *See The Wall Street Journal Europe* (Editorial), May 30, 2001; Simonian, 2001. Lower Saxony owns one fifth of VW shares, and politicians at the state ("Land") level had no desire to see shareholder pressure induce job cuts or plant closures. They were even more opposed to legal changes that might make VW vulnerable to a takeover in a consolidating global automobile sector. In short, they did not want to see what happened in the American car industry (*i.e.*, downsizing and Chrysler-style takeovers) repeat itself in Germany.

[82] *See The Financial News*, 2001.

[83] Simonian, 2001.

[84] *See* Oxford Analytica, 2001.

placed far more stringent restrictions on takeover defenses than any state in the United States.[85] American firms, by far the world's most savvy and experienced in merger and acquisition activities, have greater latitude under state corporate law to adopt poison pills and other defenses prohibited under the draft Directive. Thus, German firms would have been threatened with takeover by American firms with battle-tested financial and governance structures, hard won tacit knowledge of the offensive and defensive techniques of takeovers, and well-developed relations with financial institutions specialized in takeovers and related financial activities. The (remarkably belated) realization of how vulnerable German corporations might be to takeover by foreign firms under the draft Directive mobilized broad-based opposition and prompted the German government's shift against the directive.

Mounting opposition and the weakening of the German government's resolve in support of the Takeover Directive came as a shock to other European governments, especially those of Sweden (holding the EU presidency at the time) and the United Kingdom (the Directive's biggest proponent). The German government had been a strong proponent of the measure.[86] Chancellor Schröder's tax reforms were deliberately designed to encourage takeovers and restructuring by lowering the tax barriers to corporate sales of cross shareholdings that protected German companies from hostile bids. In fact, the proposed German takeover law, then under consideration, was modeled on the draft Directive.[87] Only a few weeks from completion of the political process, the German government shifted its position to oppose the Directive, generating accusations of betrayal from other EU governments.[88] In the Commission, the Germans were pressed by other member state governments into signing onto the Conciliation Committee draft after being outvoted initially by 14-1. The opposition then moved to the European Parliament, which was then faced with a stark choice between a neo-liberal takeover framework and an outright rejection of the draft Directive and twelve years of work.

Following the conciliation procedure in late May and early June, the Germans continued to attack the draft Directive. German Christian Democrat Klaus-Heiner Lehne was both the rapporteur for the Directive in the European Parliament and the leader of the opposition to it.

---

[85] *Cf. The Economist* (Global Agenda), June 6, 2001; Betts and Hargreaves, 2001.

[86] *See The Wall Street Journal Europe* (Editorial), 2001; *The Economist* May 10th 2001; Gledhill, 2000.

[87] In the wake of the German government's opposition to the Takeover Directive, the draft domestic legislation was changed to allow *prospective* adoption of anti-takeover defenses. This shareholder consent would have been approved in a resolution voted on at any annual general meeting of the shareholder and would then operate indefinitely to authorize management and directors to adopt anti-takeover defenses. *See* Krause, 2001.

Lehne, hailing from the area near Mannesmann's home base in Düsseldorf, argued that the draft Directive failed to address the remaining substantial differences among the company laws of different countries and that these variations would confer unfair advantages in an ensuing struggle for economic power through corporate control. Though the fear was significantly overstated, he also argued that German and other European corporations would be at a disadvantage against better-defended American firms in an international market for corporate control.[89] While Lehne emphasized that the Takeover Directive would put *German* companies at a competitive disadvantage against other European and American companies, he framed his arguments in terms of a broader reallocation of corporate and economic power that would operate unequally across EU member states. These arguments resonated with a large number of European Parliament members.

The issues stressed by Lehne dominated the debate.[90] First, the draft Directive permitted the continued deployment and use of "golden shares." This share structure, common in France and the Netherlands, would give firms possessing it a strategic advantage in the market for control.[91] Second, the fear of cross-national takeover threats from American firms and financial institutions raised by German representatives was reportedly widely shared across Europe. The opposition block used these two asymmetries to undermine support for the draft Directive in the European Parliament. Finally, the draft Directive was perceived as posing a direct threat to national sovereignty in a core area of political economic organization. Corporate governance in general, and company law in particular, links capital markets, labor relations, and the internal adjustment capacities and comparative advantages of national economies in a complex institutional framework. The Takeover Directive would have disrupted these complicated and

---

[88] *See* Hargreaves, 2001; Krause, 2001.

[89] Apparently, the countries continuing to support the Directive by and large believed they would gain more within Europe than they would lose to any American encroachments on their national firms. However, the fear of attack from well-defended American firms substantially misstated the state of American law in the most important corporate law jurisdictions. Takeover defenses are permitted in Delaware, by far the most important jurisdiction for corporate law in the United States, but fiduciary duties prevent them from *completely* blocking takeovers. In practice, they can delay and increase the premium paid for a controlling stake and this has led to the virtual disappearance of hostile takeovers in the United States since the 1980s. From this perspective, the United States (or, more accurately, the State of Delaware) arguably struck a reasonable balance with respect to hostile takeovers by making them difficult, but not impossible; the EU failed to strike a similar balance in the Takeover Directive.

[90] *See* Hong, 2001.

[91] This was especially worrying to firms in Italy and Spain under takeover threat from French companies—some recently privatized and endowed by the government with golden shares. For an account of the manipulation of share and ownership structures to ward off threats of takeover in the Netherlands and a provocative comparison with Delaware law allowing poison pills, *see* Raghavan, 2000.

potentiallycontentiousrelationshipsandthedistinctivebalanceofinterestsworkedoutbythe memberstatesduringthepost -warperiod.Thep otentialdisruptiveeffectsoftheTakeover Directivewereparticularlyseriousinneo -corporatistcountrieswithboardcodetermination.The Directive'sneutralityrequirementwouldimposeanormofshareholdersupremacyintakeover situationswhentheinterestsofshareholdersandemployeescomeintosharpestconflict. [92]From thevantagepointoforganizedlabor,socialdemocrats,andmanyChristiandemocrats,the neutralityprovisionwasnotneutralatall,butadecisiveshiftinthelegalframeworkof corporate governanceinfavorofshareholderinterestsandneo -liberalshareholdercapitalism. [93]

Inthe EuropeanParliament,onlytheliberalssupportedtheConciliationCommittee compromiseasaunitedblock(thefifty -twoMEPsaffiliatedwiththeLibera l,Democratand Reformparties). [94]Thetwomajorparliamentaryblocks,thePartyofEuropeanSocialists(the SocialDemocratswith181members)andtheEuropeanPeople'sParty(theChristianDemocratic blockwith232members),bothsplitalongnationallin es.Byatiedvoteof273to273(with22 abstentions)theEuropeanParliamentrejectedthedraftDirectiveinthefinalformadoptedbythe ConciliationCommittee. [95]AblockofMEPscomprisedofbothChristiandemocratsandsocial democrats,largelyfrom Germany,theNetherlands,Austria,Spain,andItalyembracedLehne's position.[96]Intheend,theargumentthattherewouldbeno"levelplayingfield"inthemarketfor corporatecontrolattheEuropeanorinternationallevelsundertheTakeoverDirective carriedthe day.[97]

---

[92]Hence,Scandinaviancount riessuchasSweden,wherecorporatismismanifestatthenationalandsectorallevels andlessevidentwithinthefirm,didnotdisplaythesamelevelsofhostilitytowardstheTakeoverDirectiveasdid Germany,theNetherlands,andAustria.Theselatter countrieshavewell -developedinstitutionalarrangements underpinningstable,long -termlinkagesbetweencapitalsuppliersandindustrialfirms,andamorenegotiatedand consensualformof *internal*firmgovernancebasedontripartiterelationsamongmana gement,capital,and employees.

[93]Conversely,evenintheUnitedKingdom,thesourceofthemostunequivocalpoliticalsupportfortheTakeover Directive,therewerecriticismsthatthemeasure'simpositionofmoreuniformlegalstandardswould *weaken* shareholderprotectionsunderBritishcorporategovernancerulesandderogatefromthecountry'ssovereignty. Tringham,2000(notingthatoppositiontothedraftDirectiveincreasedintheUKinresponsetoGermanandEU Parliamentattemptstoamendittoa llowfreeruseofdefensivemeasures).

[94] *See*Hong,2001.

[95]EUrulesrequiredabaremajorityintheEuropeanParliamentforadoptionoftheDirective.

[96]Unfortunately,atthetimeofthiswriting,abreakdownofthevotingintheEuropeanParliamentwasno tavailable.

[97]TheopponentswerequitepointedintheircommentsattackingtheConciliationCommittee'sdraftasfailingto addresstheseconcernsdespiteamplewarningandoutcryintheEuropeanParliament. *See*Lehne,Klaus -Heiner (EPP-ED,D),"Takeover AgreementRejectedAfterTiedVote,"Reportontakeoverbids -proposalfora13th Councildirective(PressRelease),Doc.:A5 -0237/2001(Procedure:Codecisionprocedure(3rdreading),Debate: July3,2001,Vote:July4,2001).MEPsalsostressedtheirr esentmentofandoppositiontotheperceivedheavy - handedandinflexibleattitudeoftenshownbyCouncilandCommissionintheconciliationprocess(andthereby flexedtheirowninstitutionalmuscles). *Id*.

D. Protective Convergence: The German Takeover Act

The backlash against neo-liberal takeover law reform also erupted within German domestic politics. The same interest group forces and political factions that mobilized against the EU Takeover Directive sought to protect German corporations against takeover threats by pushing for the passage of Germany's first takeover law. The Schröder government made the same calculation in the domestic arena as it had on the European Commission: it backed a moderate reform of company law governing corporate takeovers of public companies. One week after the collapse of the EU Takeover Directive, the German Bundestag passed the Securities Acquisition and Takeover Act (the "Takeover Act").[98] The statute replaced the widely derided voluntary takeover "codex" that many public companies had endorsed and routinely ignored.[99] The Finance Ministry, the government, and the Bundestag had long been at work on the statute as the means of incorporating the anticipated EU Takeover Directive into domestic law.[100] In fact, the original text of the legislation followed that of the draft Directive on the assumption its passage was only a matter of time.[101] The Mannesmann takeover and the mounting opposition to the draft EU Takeover Directive changed all this.

Compared with the politics and policy of corporate governance in the United States, state actors were far more involved in guiding and choreographing the policymaking process in Germany. What had been largely a bureaucratic and technical drafting exercise now became a highly politicized area of economic policy. The Mannesmann takeover amplified the demands for statutory regulation of takeover practices.[102] Finally, the political failure of the EU Takeover Directive placed takeover law near the center of the domestic political agenda.[103] The Schröder government once again appropriated the trappings of neo-corporatist negotiation and governance through policymaking by commission. The government appointed a 19 member blue-ribbon commission comprised of business and finance leaders, securities market officials, union representatives, and leading legal academics.[104] The commission format replicated the interest

---

[98] For an English translation of the Takeover Act, *see* www.ashursts.com/pubs/briefings.htm.
[99] Interview with Dr. Hans-Wener Neye, Bundesministerium für Justiz, Berlin, November 11, 1999 (principal drafter of the German takeover law in the Finance Ministry).
[100] *Id.*
[101] *Id.*
[102] According to Gerhard Cromme, former chief executive of ThyssenKrupp and later the chair of the government's corporate governance code commission, "The takeover came as a shock and in Germany the word 'hostile' spelt rape, pillage, destruction (of assets) and large scale redundancies." Betts, 2002.
[103] *See* Bushrod, 2001a.
[104] *See* Braude, 2000a.

groupconfigurationoftraditionalcorporatistbargainingbuta llowedthegovernmenttocontrol thepolicyagendaandrecommendationsbyselectingthegroup'smembership.

InMayof2000thecommissionreleasedareportrecommendingthatthestatuteincludea mandatorybidrulethatwouldcompelshareholdersacquirin gstakesinexcessof30%ofa corporation'sstocktomakeatakeoverbidtoallremainingshareholders, [105]a"squeezeout" provisionallowingacompulsorybuyoutofminorityshareholders,andforthefirsttime,an explicitstatutoryprovisionauthorizingma nagerstoadopttakeoverdefensesapprovedby shareholderswithintheprioreighteenmonths. [106]Thecommissionalsoacknowledgedthelegacy ofcodeterminationandorganizedlaborrelationsbynotingthattheinterestsofworkersaswell asshareholdersshou ldbetakenintoaccountinrespondingtohostilebids. [107]Yetitdidnotmake anyconcretesuggestionsastohowemployeeinterestsshouldbeenprotectedorincorporated intothetakeoverframework.Overall,manycommentatorsviewedthereportassympathe ticto takeovers.[108]

Thegovernmentpressedonwithitsefforttoenactthelawasthebacklashagainst takeoversandtheliberalizationofcompanylawgatheredmomentum.Theoppositionto takeoversacrossthepoliticalspectrum,fromcorporatemanagersbac kedbytheCDUtothe leadersoforganizedlaborsupportedbytheleft -wingoftheSPD,drovethegovernmenttoaccept expandedmanagerialpowerstoadopttakeoverdefenses.Thedomesticpoliticsoftakeoverlaw ranparalleltothebattleovertheEUDire ctive.Managersseekingdefensesagainstraidersand unionsdemandingprotectionforjobsandcodeterminationpoliticallyoverranthelargebanks andshareholdersgroupsseekingtofacilitatetakeoversandconsolidatedthevictorytheyhad wonintheEuro peanParliament. [109]Managerswongreaterleewaytoadopttakeoverdefenses andlaborsecuredgreaterproceduralandinformationalrights.

---

[105]Mandatorybidrules,widelymootedthroughoutEurope,isdesignedtodistributethecontrolpremiumtoall shareholdersbyrequiringownersacquiringacontrolblock(*e.g.*,30%)tothemmakeanoffer totheremaining shareholdersonsimilarterms.Thislegalrulemayencouragethedevelopmentoftenderoffersasameansof changingcorporatecontrol,butdiscouragethetraditionalEuropeanmechanismforcontroltransfers —thesaleof controllingequit ystakesbyblockholdersinexchangeforacontrolpremium.

[106] *Seeid* .

[107]ChancellorSchrödersupportedthisbalancingofinterestsobliquelybyexpressingconcernthatinstitutional investorsbehave"responsibly"intakeoversituationsandthatacquirers committhemselvestodevelopingthe purchasedfirms. *Seeid* .

[108]Braude,2000b.

[109] *See*BraudeandHong,2001,Barbier,2001a.

TheGermancabinetapprovedtheSecuritiesAcquisitionandTakeoverActonJuly11, 2001,oneweekaftertherejectio noftheEUTakeoverDirective. [110]TheBundestagapprovedthe legislationonNovember15,2001anditcameintoeffectonJanuary1,2002.TheTakeoverAct coverspublictenderoffers,takeoveroffers(offerstoacquire30%ormoreofapublicfirm's votingstock),andmandatoryoffersforremainingsharesoncetheofferor'sstakereachesthe 30%controlthreshold.TheActincorporatedmostoftheTakeoverCommission's recommendations.[111]Itimposesminimumbidrequirements,aprovisioncompellinga mandatorytakeoverbidonceanacquirer'svotingstakereachesa30%threshold,asqueezeout rulethatallowsamajorityowning95%ormoreofacorporationtobuyouttheremaining minorityshareholders. [112]TheTakeoverActalsoextendedtheBAWe'sregulatoryaut horityto corporatetakeovers. [113]

TheTakeoverActcontainsageneral"dutyofneutrality"thatprohibitsthemanagement boardfromtakinganyactionthatwouldpreventthesuccessofthehostilebid. [114]However,the statuteexpandedthelatitudeofmanagemen ttodeploydefensivetacticsagainstahostile takeover.Managementmayseekshareholderauthorizationtousespecifieddefenses.These resolutionsarevalidforuptoeighteenmonths,requirea75%supermajorityvote,andthe supervisoryboardmustapp roveanydeploymentofthesedefenses. [115]Moreimportantly,the dutyofneutrality"doesnotapplytoactsthatwouldalsohavebeenperformedbyaprudent managerofacompanynotaffectedbyatake -overoffer,thelookingoutforacompetingoffer, *aswel lasactsapprovedbythesupervisoryboardofthetargetcompany* ."[116]Thisprovision grantsthesupervisoryboardpotentiallyvastdiscretiontodefendagainsttakeover,similartothe reallocationoflegalauthoritytotheboardsofAmericancorporations duringthe1980s.Yetthe ActdoesnotexplicitlyauthorizeaGermanequivalentofthepoisonpilldefensecommonin Americanpracticeandthelegalstatusofsuchmechanismsremainssubjecttosomedoubt. [117]

---

[110]Williamson,2001b;Braude,2001b;BBC,July11,2001;Wood,2001.

[111]ForthetextoftheAct, *see* www.ashursts.com/pubs/briefings.h tm.Foroverviewsofthelegislation, *see* Strelow andWildberger , 2002;Osborne&Clarke, 2002; Rissel, 2002;Zehetmeier -MuellerandUfland,2002.

[112]ThewarmwelcomefortheTakeoverAct'ssqueezeoutprovisionsasaboontoMBOactivityindicatesthe politicalandeconomicambiguityofthelaw. *See*Hobday,2001.

[113]SecuritiesAcquisitionandTakeoverAct,§§4 -9.

[114]"[T]hemanagingboardofthetargetcompanymaynotperformanyactswhichmightresultinthesuccessofthe offerbeingprevented."Securiti esAcquisitionandTakeoverAct,§33.1.

[115]SecuritiesAcquisitionandTakeoverAct,§33.2.

[116] *Id*.§33.1; *seealso* Braude,2001a.

[117]Withoutactivistcourtstoclarifythecomplexlegalissuesandambiguousstatutoryrules,theapplicationofthe Actwillb etroublesome.Inalllikelihood,thecourtswillconstruetheAct'srequirementof75%shareholder

Yet the Takeover Act does not alter the fiduciary obligations of directors to act in the shareholders' best interests or introduce measures to increase the supervisory board's independence from management. Given the conceptual and practical difficulties of relying on fiduciary duties to vindicate shareholder interests in a codetermined governance regime, the drafters of the law relied instead specific bidding procedures and disclosure requirements on takeovers. The details of takeover bids must be fully disclosed in a filing with the BAWe (similar to an SEC filing in the United States) and through publication, along with any plans the acquirer has for the firm following a change of control.[118] The target's management must respond with a public report assessing the adequacy of the offer and the bidder's business strategy. In addition, the bid must remain open between four and ten weeks, with an additional two week "sweep up" period for dilatory shareholders to tender their shares. Far from recognizing shareholder primacy, the Takeover Act obliges both the offeror and the target's management to disclose information to either the works council or directly to the employees concerning the terms of the offer and its implications for the firm and employees and their collective representation.[119] Thus, the Act makes use of and may reinforce the institutions of works council codetermination even as it expanded the supervisory board's power.

VII. Conclusion

The politics of German corporate governance reform and the spilling over of that politics into the EU illustrate political tensions inherent within the processes of economic reform. Interests, interest groups, and ideological commitments collide and constrain attempts to advance agendas of structural change. The KonTraG reforms resulted from a combination of entrepreneurial state actors and interest group politics. This combination mobilized a significant, though diffuse, populist resentment of concentrated financial capital and economic power and interest group alignments favoring more liberal economic policies in the area of corporate governance and company law. The populist element of the political agenda was used to place the issue of company law reform on the policy-making agenda, but then abandoned in the course of political compromise over the legislation. During these negotiations economic interests came

approval for capital increases relating to takeover defenses to cover poison pills (even though American practice clearly shows that no capital is raised or anticipated from these plans).

[118] *See id.* §§ 11, 14.

to the fore and determined the final shape of the legislation. The legislation stripped the large German banks, the original targets of populist ire, of the mechanisms of leverage and corporate control that they were willing to abandon. Labor was able to block changes that threatened to weaken supervisory board codetermination. However, the liberal shift in German domestic policy represented by the KonTraG caused complications in European politics.

The genesis of the stunning defeat of the EU Takeover Directive, and the resulting setback for the European Commission's capital market integration agenda and the cause of economic liberalism in the EU, resides in the tensions within German policy and politics that had been bubbling underneath the reform agendas of the country's political parties. The irony of the battle over the Takeover Directive was that Germany did *not* switch its position on the Takeover Directive because it was hostile to economic modernization and liberalization. Rather, it was *because domestic reforms had already liberalized the legal structure of corporate governance* to a significant degree and other member states had not undertaken similar steps. Germany's reforms during the late 1990s were highly coordinated. The EU takeover proposal dealt with the subject as if in a vacuum and failed to recognize and accommodate the broader systemic character of corporate governance reform at the national level. Accordingly, the Takeover Directive would have created undesirable —and indefensible —inequalities in the defense mechanisms available to the corporations of different member states. The European Commission refused to acknowledge or address this issue that was of paramount importance to domestic political and economic actors.

Without question, the German public and large segments of the economic and political elites were ambivalent about economic liberalism and are largely hostile to the very idea of takeovers. However, this ambivalence and hostility was not sufficient to block the string of substantial economic reforms of 1998 through 2000 that have incorporated Anglo-American legal structures and principles within German corporate governance conflicts to an unprecedented degree. However, once the implications of these reforms within the broader context of the European and global political economies became clearer, German politics reversed course and unleashed a backlash against the American model of corporate law and the market for

[119] *See id.* §§ 10.5, 11.2.6.2, 27. Labor is also entitled to two representatives on the BAWe's thirteen-member "advisory board" on takeovers created pursuant to the Takeover Act, § 5.1.

corporatecontrol.Ironically,thisbacklashtookitsfinalforminthelegislativesanctionofthe veryanti -takeoverdefensescommonlyusedintheUnitedStates.

JustasBaumsandBuryinGermanyhadcalculatedin1998thattheycouldmobilizeboth eliteandpopulist *support*forliberalizationinframingtheKonTraGdebate,Klaus -HeinerLehne intheEuropeanParliamentandacross -classcoalitionofSocialDemocratsandChristian DemocratsinGermanyduringmid -2001mobilizedthesamecombinationofpopul arandelite supportinGermanyandacrossEuropeto *oppose*furtherliberalization.Inthedebatesoverthe KonTraG,theEUTakeoverDirective,andtheGermanTakeoverLaw,advocatesoflegalchange heldoutthespecterofconcentratedfinancialpoweras athreattoprosperityandajustsocio - economicorder.Whattheadvocatesofneo -liberalismintheEUdidnotcountonadequately wasthatthisswordofpseudo -populismandinterestgrouppoliticswouldprovetobedouble edged.

References

Albert,Mich el, *CapitalismAgainstCapitalism* ,translationbyPaulHaviland(London:WhurrPublishers, 1993)

Barbier,HansD., “Germany'sIntricateWeb ,” *FrankfurterAllgemeineZeitung* ,July9,2001 ,available onlineat,http://www.faz.com(2001a)

BaumsCommissionP ressRelease,GermanFederalGovernment,PressemitteilungNr.321/00, http://eng.bundesregierung.de/frameset/index.jsp,KonstituierendeSitzungderExpertenkommission „CorporateGovernance:Unternehmensführung -Unternehmenskontrolle –Modernisierungdes Aktienrechts"(Wednesday,June21,2000)

BBC, Germanytocurbhostiletakeovers, Wednesday,11July,2001,availableonline, http://news.bbc.co.uk/hi/english/business/newsid_1433000/1433380.stm

Betts,Paul,“Europe'sCapitalistsSurveyaLevelPlayingField ,” *FinancialTimes* , May31,2002, p.13

Betts,PaulandDeborahHargreaves,“NoWayIn,” *FinancialTimes* ,May2,2001

Braude,Jonathan,“GermanyToSwallowPoisonPills,” *TheDailyDeal* ,November14,2001(2001a)

Braude,Jonathan,“GermanyApprovesNew TakeoverCode,” *TheDailyDeal* ,July11,2001(2001b)

Braude,Jonathan,“GermanPanelOffersProposedTakeoverRules,” *TheDailyDeal* ,May17,2000 (2000a)

Braude,Jonathan,“GermanySeemsReadytoAcceptHostileTakeovers,” *TheDailyDeal* ,May23,200 0 (2000b)

Braude,JonathanandVictoryaHong,"TakeoverdirectivedividesGermany," *TheDailyDeal* ,May23, 2001

Breuer,Rolf -E.,"TheRoleofFinancialIntermediariesandCapitalMarkets,"inHopt,KlausJ.,Hideki Kanda,MarkJ.Roe,EddyWymeersch,an dStefanPrigge,eds., *ComparativeCorporateGovernance: TheStateoftheArtandCurrentResearch* (NewYorkandOxford:OxfordUniversityPress,1998)

Bushrod,Lisa," GermanyandTakeoverCodes," *EuropeanVentureCapitalJournal,* November 1,2001, availableat
http://www.buyoutsnewsletter.com/evcj/protected/ctryreps/ZZZSH6NLITC.html(2001a)

Bushrod,Lisa, " Buyouts:StillAwaitingaBoom," *EuropeanVentureCapitalJournal,* November 1, 2001,availableat http://www.buyoutsnewsletter.com/evcj/protected/ctryreps/ZZZKH6NLITC.html (2001b)

Cioffi,JohnW., ***PublicLawandPrivatePower:TheComparativePoliticalEconomyofCorporateGovernance intheUnitedStatesandGermany*** **,DoctoralDissertation,DepartmentofPoliticalScience,Universityof California,Berk eley(2002)**

Cioffi,JohnW., *GoverningGlobalization?TheState,Law,andStructuralChangeinCorporate Governance*,BritishJournalofLawandSociety,vol.27,pp.572 -600(Winter2000)(2000a)

Cioffi,JohnW., *StateoftheArt:AReviewEssayon* *ComparativeCorporateGovernance:TheStateof theArtandEmergingResearch* ,AmericanJournalofComparativeLaw,vol.48,pp.401 -434(Fall2000) (2000b)

Deeg,Richard, *FinanceCapitalismUnveiled:BanksandtheGermanPoliticalEconomy* ,(AnnArbor: UniversityofMichiganPress,1999)

TheEconomist "TakeoverTroubles,"May10th2001

TheEconomist ,"ShoppingaroundinEurope"(GlobalAgenda),June6,2001

TheFinancialNews ,"HostileBidsGiveWaytoMillenniumSensitivities,"June11,2001,availableon Westlaw,2001WL12506312

GermanLawJournal ,InterviewwithProfessorDr.TheodorBaums,ReformingGermanCorporate Governance:InsideaLawMakingProcessofaVeryNewNature,vol.2,no.12,(July16,2001)

Gledhill,Dan,"TheThingIs...HostileTakeo vers," *TheIndependent –London* ,December17,2000 (BusinessSection),availableonWestlaw,2000WL29496281

Gordon, JeffreyN. ,*PathwaystoCorporateConvergence?TwoStepsontheRoadtoShareholder CapitalisminGermany:DeutscheTelekomandDaimlerCh rysler*, ColumbiaUniversitySchoolofLaw, CenterforLawandEconomicStudies, WorkingPaperNo.161(January31,2000);alsopublishedin ColumbiaJournalofEuropeanLaw,vol.5,no.219(Spring1999)(SymposiumIssue)

GovernmentCommissiononCorporate Governance(BaumsCommission), *GermanCorporate GovernanceCode* (Draft,datedDecember12,2001)

Hargreaves,Deborah,"GermanyBacksoutofEUCorporateTakeoverAccord," *FinancialTimes* ,May1, 2001

Hong,Victorya,"VoteonEuropeanTakeoverLawHeats Up," *TheDailyDeal* ,Monday,July2,2001, availableonWestlaw,2001WL20235168

Jahn,Joachim," TheodorBaums:TheChancellor'sLegal," *FrankfurterAllgemeineZeitung* (September 20,2001)

Jenkinson,TimandAlexanderLjungqvist,"TheRoleofHostileSt akesinGermanCorporate Governance,"draftpaperdated,August17,1999

Köke,Jens," ControlTransfersinCorporateGermany:TheirFrequency,CausesandConsequences," ZEWDiscussionPaperNo.00 -67,CentreforEuropeanEconomicResearch,Mannheim,Germa ny (December2000)

Krause,KlausPeter,"ShareholdersMaySoonHavetheRighttoBlockTakeoversinAdvance," *FrankfurterAllgemeineZeitung* (EnglishEdition),May8,2001

Lazonick, William and Mary O'Sullivan, *Corporate Governance and Corporate Employme nt: Is ProsperitySustainableintheUnitedStates?* ,JeromeLevyEconomicsInstitute,WorkingPaperNo.183 (January1997)

Lehne,Klaus -Heiner,"TakeoverAgreementRejectedAfterTiedVote,"Reportontakeoverbids - proposalfora13thCouncildirective (PressRelease),Doc.:A5 -0237/2001(Procedure:Codecision procedure(3rdreading),Debate:July3,2001,Vote:July4,2001)

Mülbert,PeterO.,"BankEquityHoldingsinNon -FinancialFirmsandCorporateGovernance,"inHopt, KlausJ.,HidekiKanda,Mark J.Roe,EddyWymeersch,andStefanPrigge,eds., *ComparativeCorporate Governance:TheStateoftheArtandCurrentResearch* (NewYorkandOxford:OxfordUniversityPress, 1998)

Osborne&Clarke," NewGermanSecuritiesAcquisitionandTakeoverActEnacted ,"January2002, availableonline,http://www.osborneclarke.com/publications/text/germansecurities.htm

OxfordAnalytica,"EUROPEANUNION --TakeoverTensions," *InPerspective,TheAnalyticaWeekly Column*,May24,2001

Pistor,Katerina,"Co -determination inGermany:ASocio -PoliticalModelwithGovernance Externalities,"inMargaretM.BlairandMarkJ.Roe,eds., *EmployeesandCorporateGovernance* (Washington,DC:BrookingsInstitutionPress,1999),originallypublishedin *CorporateGovernance Today CorporateGovernanceToday* (NewYork:ColumbiaUniversitySchoolofLaw,May1998) (volumepublishedbytheSloanProjectonCorporateGovernanceatColumbiaLawSchool)

Porter,Michael, *TheCompetitiveAdvantageofNations* (NewYork:FreePress,1990)

Raghavan,Anita,"Deals&DealMakers:NetherlandsRemainsCooltoInvestors'Concerns," *TheWall StreetJournal* ,December22,2000,availableonWestlaw,2000WL -WSJ26620875

Rissel,Dirk ,“OverviewofthenewGermanTakeoverLaw,” *EurojurisLawJournal* ,March2002, availableonline, http://www.eurojurislawjournal.net/RA/Rissel/Overview-of-the-new-German-Takeover-Law.html

Roe,MarkJ., *PoliticalPreconditionstoSeparationofOwnershipFromControl:TheIncompatibilityof the American Public Firm with Social Democracy* (unpublished draft, Columbia Law School, June 1, 1999)

Roe,MarkJ. ,“CodeterminationandGermanSecuritiesMarkets,”inHopt,KlausJ.,HidekiKanda,Mark J.Roe,EddyWymeersch,andStefanPrigge,eds., *ComparativeCorporateGovernance:TheStateofthe ArtandCurrentResearch* (NewYorkandOxford:OxfordUniversityPress,1998)

Roe, Mark J., *Strong Managers, Weak Owners: The Political Roots of American Corporate Finance* (Princeton,NJ:PrincetonUniversityPress,1994)

RoeMarkJ., *SomeDifferencesinCorporateStructureinGermany, Japan, andthe UnitedStates* ,Yale LawJournal,vol.102,p.1927(1993)

Roe,MarkJ., *APoliticalTheoryofAmericanCorporateFinance* ,ColumbiaLawReview,vol.91,p.10 (1991)

Seibert,Ulrich, *ControlandTransparencyinBusiness(KonTraG):CorporateGovernanceReformin Germany*,EuropeanBusinessLawReview,pp.70-75(1999)

Simonian,Haig,“BerlinBowstoPressure,” *FinancialTimes* ,May2,2001

Soskice, David, “Divergent Production Regimes: Coordinated and Uncoordinated Market Economies in the 1980s and 1990s,” in Kitschelt, Herbert, Peter Lange, Gary Marks, and John D. Stephens, eds., *ContinuityandChangeinContemporaryCapitalism* (Cambridge:CambridgeUniversityPress,1999)

Soskice,David,"TheInstitutionalInfrastructureforInternationalCompetitiveness:AComparative AnalysisoftheU.K.andGermany,"inA.B.AtkinsonandR.Brunetta,eds., *TheEconomicsoftheNew Europe*(InternationalEconomicAssociationConferenceVolume:1992)

Streeck, Wolfgang, "Codetermination After Four Decades," in Wolfgang Streeck, ed. *Social Institutions andEconomicPerformance:StudiesofIndustrialRelationsinAdvancedCapitalism* (1992)

Streeck,Wolfgang,"OntheInstitutionalConditionsofDiversifiedQualityProduction,"inEgonMatzner and Wolfgang Streeck, eds., *Beyond Keynesianism: The Socio-economics of Production and Full Employment*(Brookfield,VT:Elgar,1991)

Strelow,MarkusandJanWildberger ,“ TheNewGermanTakeoverAct -ANewOpportunityforPrivate Equity?” *ThompsonVentureEconomics* ,April 29,2002,availableonline, http://www.ventureeconomics.com/buy/protected/ZZZ4HGCLBZC.html

Tringham,Melanie,“BidBattlesUnderAttack,” *TheTimesofLondon* ,December21,2000,availableon Westlaw,2000WL28139519

Vagts,DetlevF., *Reformingthe"Modern"Corporation:Perspectives fromtheGerman,* HarvardLaw Review,vol.80,p.23(1966)

TheWallStreetJournalEurope ,"Takeovers?Nein!"REVIEW&OUTLOOK(Editorial),May30,2001, availableonWestlaw,2001WL -WSJE21829756

Wenger,EkkehardandChristophKaserer,"TheGermanSyst emofCorporateGovernance –AModel WhichShouldNotBeImitated,"in StanleyW.BlackandMathiasMoersch,eds., *OECDCountriesin CompetitionandConvergenceinFinancialMarkets* (1998)(1998a)

Wenger,EkkehardandChristophKaserer,"GermanBanksand CorporateGovernance --ACriticalView," in Hopt,KlausJ.,HidekiKanda,MarkJ.Roe,EddyWymeersch,andStefanPrigge,eds., *Comparative CorporateGovernance:TheStateoftheArtandCurrentResearch* (NewYorkandOxford:Oxford UniversityPress,1998) (1998b)

Williamson,Hugh, "GermanyActstoLimitHostileTakeovers, " *FinancialTimes* ,July 11,2001, p.10,availableonlineat,http://www.ft.com(2001b)

Wood,RobertW.,"GermansintheNewsAgain," *M&ATaxReport,* vol.10,no.2,p.8(September200 1)

Zehetmeier-Mueller,RuthandRichardUfland,"ANewEraforPublicTakeoverTransactionsin GermanyHasBegun,"LegalWeekGlobal,April17 -May14,2002,availableonline http://www.legalweek.net/ViewItem.asp?id=8571&Keyword=takeover

Ziegler,J.Nich olas, *CorporateGovernanceandthePoliticsofPropertyRightsinGermany* ,Politics& Society,vol.28,no.2,pp.195 -222(June2000)

Zysman,John, *Governments,Markets,andGrowth* ,(Ithaca:CornellUniversityPress,1983)

Interviews

HelmutAchatz,Deu tschesAktieninstitut(DAI),Frankfurt,December6,1999

AnonymousinterviewswithGermanlaborunionofficials,summer1999,winter1999,andsummer2000

Prof.Dr.TheodorBaums,UniversityofOsnabrück,Osnabrück,July13,1999

MarcusBecker -Melching,BundesverbanddeutscherBanken(BDB),Berlin,November11,1999

OttoFricke,AttorneyatLawandCounselor,FDP,Berlin,November1,1999.

Dr.RainerFunke,MemberoftheBundestag,FDPBundesfraktion,Berlin,November2,1999

MarkusHerdina,Deutsch esAktieninstitut(DAI),Frankfurt,December6,1999

Dr.RolandKöstler, DeutscherGewerkschaftsbund (DGB -theGermanFederationofTradeUnions)and HansBöcklerStiftung,Düsseldorf,December12,1999

Dr.RolandKöstler, DeutscherGewerkschaftsbund (DGB -theGermanFederationofTradeUnions)and HansBöcklerStiftung,formersupervisoryboardmemberofMannesmann,AG,Düsseldorf,July18, 2000

Dr.UlrichSeibert,LeiterdesReferatsfürGesellschaftsrechtundUnternehmensverfassung,Ministryof Justice,Berlin,July5,1999

PeterM.Wiesner,HeadofLegalAffairs,Legal,CompetitionPolicy,andInsuranceDepartment, FederationofGermanIndustry(BDI),Brussels,Berlin,July11,2000

StatutesandProposedLegislation

AmendmenttotheSecuritiesTradin gActbyArticle3oftheThirdFinancialMarketPromotionAct (GesetzzurweiterenFortentwicklungdesFinanzplatzesDeutschland,Drittes Finanzmarktförderungsgesetz)of24March1998(FederalLawGazettePartIp.529)

AmendmentoftheSecuritiesTradin gAct(Wertpapierhandelsgesetz)byArticle2oftheLaw ImplementingtheECDepositGuaranteeDirectiveandInvestorCompensationDirectiveof16July1998 (FederalLawGazetteI,p.1842)

AmendmenttotheSecuritiesTradingActbyArticle2oftheLawIm plementingECDirectivesforthe HarmonisationofRegulatoryProvisionsintheFieldofBankingandSecuritiesSupervision(Gesetzzur UmsetzungvonEG -RichtlinienzurHarmonisierungbank -undwertpapieraufsichtsrechtlicher Vorschriften)of22October1997 (FederalLawGazettePartIp.2518)

AmendmenttotheSecuritiesTradingActbyArticle16oftheJudiciaryNotificationActandtheAct AmendingCostLawProvisionsandotherLaws(JustizmitteilungsgesetzundGesetzzurÄnderung kostenrechtlicherVorsc hriftenundandererGesetze,JuMiG)of18June1997(FederalLawGazettePartI p.1430)(enteredintoforce1June1998)

CodeterminationAct(GesetzuberdieMitbestimmungvonArbeitnehmern)ofMay4,1976(BGBl.I 1153),asamendedOctober28,1994(BGB l.I3210)("MitbestG")

CorporateControlandTransparencyAct(GesetzzurKontrolleundTransparenzim Unternehmensbereich)of27April1998,FederalLawGazette,PartI,p.786(Gesetzvom27.4.1998, BGBl.I,S.786vom30.4.1998)("KonTraG")

ProspectusAct(Verkaufsprospektgesetz)asannouncedon9September1998,FederalLawGazette,Part I,p.2701,aslastamendedbyArticle2oftheActontheFurtherPromotionofGermanyasaFinancial Centre(ThirdFinancialMarketPromotionAct)of24March1998 (FederalLawGazetteIp.529)

SecuritiesAcquisitionandTakeoverAct(ActontheRegulationofPublicOffersfortheAcquisitionof SecuritiesandCorporateTakeovers),adoptedNovember15,2002,effectiveJanuary1,2002,unofficial translationproduc edbyAshurstMorrisCrisp,availableonline,www.ashursts.com/pubs/briefings.htm

SecuritiesTradingAct(Wertpapierhandelsgesetz)ofJuly26,1994,§§3 -11(FederalLawGazette,PartI, p.1749),promulgatedasArticleIoftheSecondFinancialPromotion Act(Gesetzüberden WertpapierhandelundzurÄnderungbörsenrechtlicherundwertpapierrechtlicherVorschriften,Zweites Finanzmarktördnungsgesetz)("WpHG")

StockCorporationAct (Aktiengesetz),1965BGB1.I1089,amendedby1994BGB1.I48("AktG").

ThirteenthCouncilDirectiveonCompanyLawConcerningTakeoverBids,OJC64,14.3.1989

ThirteenthCouncilDirectiveonCompanyLawConcerningTakeoverBids,EuropeanCommission's AmendedProposal,10September1990,OJC240,26.9.1990

ThirteenthCounci lDirectiveonCompanyLawConcerningTakeoverBids,SecondProposalfora ThirteenthDirectiveonCompanyLawConcerningTakeoverBids,OJC162,6.6.1996

ThirteenthCouncilDirectiveonCompanyLawConcerningTakeoverBids,ThirdAmendedProposalfor a ThirteenthDirectiveonCompanyLawConcerningTakeoverBids,OJC378,13.12.1997