PANEL DISCUSSION ON CORPORATE GOVERNANCE: U.S., GERMAN, AND JAPANESE PERSPECTIVES

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1. Dedication

Noyes Leech retires from the faculty of the University of Pennsylvania Law School after 37 years as a distinguished scholar, superb teacher, and invaluable colleague. It is particularly fitting that the student editors of the Journal decided to dedicate this issue to Professor Leech because he is one of the founders of the Journal and of the International Faculty for Corporate and Capital Market Law, whose work provided the foundation upon which the Journal was built.

The International Faculty, a distinguished group primarily of academics from nine countries, was created as a response to the rapid internationalization of the capital markets. Professor Leech thought it desirable to establish a living resource to accumulate and make available, on a timely basis, knowledge and expertise relevant to the major participants in the developing international financial markets.

The concept of the International Faculty attracted Professor Leech, because it allowed common issues to be pursued in a particularized and practical fashion. Loose, general statements annoy Professor Leech. In the setting of the International Faculty, statements could be pursued in detail until the relevant insight was cleanly articulated. The process of questioning allowed all who participated in the discussion to understand precisely the extent to which, for example, our Swiss colleague, Alain Hirsch, might object to the notion of required disclosure of financial information about a publicly held company and the circumstances in the Swiss experience which accounted for his objections.

The discussion which constitutes this article reflects Professor Leech's approach to teaching. A comparative analysis of Japanese, German, and

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American law, as it relates to certain aspects of corporate governance, is developed by forcing a lawyer familiar with each system to address common, concrete hypotheticals. By requiring specific answers and supporting explanations, similarities and differences in the system emerge with clarity. If there were more hypotheticals and someone to probe the soft spots in the answers initially presented, we would have a pretty good picture of how Professor Leech likes to teach a course and we would also understand why we at the University of Pennsylvania Law School regard him as one of our greatest teachers.

2. Introduction

This panel will deal with corporate governance [1]. This notion refers to the distribution of decision-making powers in large enterprises. The basic problem is that those who make these decisions should make them not only and not even primarily for themselves but also for other people. Therefore, it can be generally assumed that we are all, from whatever legal system we come, interested in having some mechanisms that insure the accountability of corporate decision making.

How we view these mechanisms and what we expect from them may depend very much on how we view the big enterprise:

- We could perceive it as an organization which is primarily determined by market forces. This organization may in some points not work as effectively as we wish. We therefore could have legal rules in order to improve economic efficiency;
- We could also see the enterprise as a social and political institution having an impact not only on markets but also on social structures like the political process and behavioral attitudes (the way people think and act). We therefore may want legal rules in order to fit the enterprise into the patterns of our society. It is obvious that this means a different function of law.

Our discussion should explore how important legal systems actually deal with these issues.

3. Background on German Law

Professor Kuebler:

Let me summarize some of the aspects of German corporate law in three points.

My first point deals with statistics. In Germany, there are only about 2,000 stock corporations (Aktiengesellschaften, AG) [2] compared to close to 300,000 limited liability companies (Gesellschaften mit beschränkter Haftung, GmbH)
The transfer of shares in a GmbH requires a contract concluded before a notary public; therefore, the GmbH can only be used as a closed corporation. However, many medium-sized and even some large enterprises are still run in the legal form of a limited partnership.

There are only about 450 corporations listed on one of the stock exchanges and there is no over-the-counter market. For about sixty years — from the beginning of the First World War to the mid-1970s — virtually no business has gone public. There have been some changes during the last few years: for example, companies like Springer (the largest newspaper publisher), Nixdorf (a fast-growing computer producer), and Porsche (until recently the last privately-owned car company) are now listed on the stock exchange.

Among the 450 companies listed on a stock exchange, there are many which are controlled by individuals, families or other enterprises. Thus, there is a very small number of truly public corporations, maybe twenty or twenty-five (the number depends somewhat on the definition given to the notion of a "public" corporation). These corporations are the big names in German business, such as Deutsche Bank, Allianz, Daimler-Benz, and Bayer. Thus, the public corporations are a small community in a comparatively small country; the scenario is quite different from that in the U.S.

My second point relates to law. German law requires a mandatory two-tier board system for stock corporations; there has to be a management board (Vorstand) as well as a supervisory board (Aufsichtsrat).

The managing board actually runs the business; it represents the corporation in all transactions and decides its day-to-day activities. The members of the managing board are appointed by the supervisory board for a maximum of five years and the appointment can be renewed. That, of course, happens in most cases.

The supervisory board was originally designed as a strict institutionalization of the independent or outside director; all its members were elected by the shareholders in the annual meeting. Today this is true only for one-half of the members. The other half is elected by the employees of the enterprise. This practice is the key element of the German system of worker codetermination. It began more than sixty years ago and since then four codetermination laws have been enacted. It can have an important impact on corporate decision making as well as on labor relations.

My third point is that the German stock corporation is normally not involved in litigation, and this is particularly true of the big public corporations. There are only a few cases and that means that there is not much law. Apart from the small number of stock corporations, there are two reasons for this lack of activity: first, there is virtually no derivative suit, i.e., a single shareholder cannot sue the managing board on behalf of the corporation; secondly, there is no contingency fee and thus no incentive for lawyers to seek conflicts and commence litigation.
4. Background on Japanese Law

4.1. Basic Structure of the Japanese Legal System

Mr. Shapiro:

The present structure of the Japanese legal system has evolved over the past 100 years. It represents a unique case of a voluntary importation of a group of foreign legal institutions superimposed on an indigenous cultural base.

Japan is basically a Civil Code country rather than a country whose legal system is based on common law. In the early years after the Meiji Restoration in 1868 [10], it came under the French influence. As a result, the Civil Code of 1890 and the Penal Code of 1882 were French imports [11]. The French phase ended and the German phase began just before the turn of the century [12]. Thereafter, the German influence predominated until after World War I [13], during which the Japanese were on the side of the Allies and fought against Germany.

In between the two World Wars, the Anglo-American influence predominated, resulting in the importation of Anglo-American trust law into Japan [14]. During the 1930s and 1940s, Japan turned inward and sought to rely more on its own indigenous, cultural institutions and sought to impose a Japanese national character on the legal system [15].

After World War II, with the total destruction of Japan and the occupation by the United States for a period of seven years, the legal system underwent extensive changes influenced by the American occupiers [16]. This was especially true in the corporate and tax fields as well as in the antitrust and securities fields [17].

The Japanese courts are divided into the familiar three-tier structure of district courts, intermediate appellate courts, and a Supreme Court composed of fifteen justices [18]. While Japan experimented with the jury system in criminal cases between 1923 and 1943 [19], juries have not been used traditionally and are not used today.

Cases have precedential value and this is not totally unfamiliar to the Japanese mind, inasmuch as during the 250-year period before the Restoration of 1868, judicially-made law played an important part in the Japanese legal system [20].

Japan has had two written constitutions in modern times: the first, modeled after the German Constitution, was promulgated in 1889 (Meiji Constitution); the second, an American draft, was promulgated in 1946 under the U.S. Occupation (Showa Constitution) [21]. There are those in Japan who believe it is time for the Japanese to draft their own charter.

4.2. The Japanese Legal Profession

The Japanese Bar is essentially a barrister's bar. In creating the new profession of bengoshi (counsel) [22], the Japanese used the English barrister
and the French avocat (advocate) as their model. The first bar associations were formed in 1880 [23] and the first law regulating the profession was adopted in 1893 [24]. Japanese barristers are educated on the European model, i.e., law faculties are departments in undergraduate universities. After four years in a faculty of law, a person wishing to be a judge, a prosecutor (only approximately one percent do so) [25], or a barrister has to pass the national bar examination and then receive special training at the Legal Training and Research Institute for two years [26]. Thus, the Japanese Bar has been kept artificially small.

4.3. Japanese Attitudes Toward Law

The Japanese, like the Chinese, dislike abstract principles. They believe law is primarily an expedient to satisfy human needs, which is an attitude inherited from the Confucian tradition [27]. Law is regarded as a nuisance to be avoided, if possible [28]. In this connection, formalism should not be confused with legalism; while the Japanese are formalists, they are not legalists. Therefore, it is important to understand that the behavioral answer and the legal answer may be different, i.e., the culture and psychology may dictate one mode of behavior while the law suggests another.

5. Panel Discussion

5.1. Hypothetical Number One

The Chief Executive Officer (CEO) of Alpha, a large publicly held corporation, is an alumnus of Epsilon University. Alpha’s executive offices and manufacturing sites are located far away from Epsilon. Epsilon asks Alpha for a contribution of $100,000 to the endowment for its library. Would it be legally proper for Alpha to make the contribution? Is it likely that Alpha would make the contribution?

5.1.1. Dean Mundheim’s Response

The relevant U.S. law for answering this hypothetical can be found in the statutes and decisions of the state in which Alpha is domiciled. Although state corporation laws generally view the business corporation as having the objective of conducting its business with a view to enhancing corporate profit and shareholder gain, these laws increasingly recognize that even where corporate profit and shareholder gain are not enhanced, the corporation may properly expend “a reasonable amount of resources for public welfare, humanitarian, educational and philanthropic purposes” [29]. This development reflects the American desire to see diversity and decentralization in the pursuit of educa-
tional and philanthropic activity. It would be difficult to achieve the goals of diversity and decentralization without encouraging corporate generosity.

A gift by Alpha to the library at Epsilon University might even be sustained under the more traditional view that corporations may only act in a way which enhances shareholder economic interests. For example, in a well known case, *A.P. Smith Manufacturing Co. v. Barlow* [30], the New Jersey Supreme Court was asked to examine the propriety of a corporate contribution to Princeton University's annual giving campaign. The court sustained the gift. It found that the corporation benefited at least indirectly from making the gift because free, non-governmental educational institutions are essential in fostering an economic and social environment suitable for private business enterprise. Such a broad articulation of the benefits standard appears to allow a broad variety of corporate contributions to pass judicial muster as an appropriate object of corporate concern.

Alpha will probably be limited to holding its contribution to Epsilon to a reasonable amount [31]. Although there are no firm benchmarks to measure a reasonable amount [32], one guideline would be the ten percent of taxable income which a corporation may deduct for federal income tax purposes [33]. In fact, total charitable giving for corporations in the U.S. tends to be closer to one percent than ten percent of taxable income [34].

The last part of the hypothetical asks whether it is likely that Alpha would make the contribution. Corporations are major supporters of universities in the United States [35]. The interest of Alpha's CEO should be very helpful in securing the contribution for Epsilon. However, there is a disposition to link corporate contributions to institutions and projects which have some relationship to the interest of the corporation, its employees or other important constituencies.

5.1.2. Professor Kuebler's Response

A situation like the one presented in the first hypothetical has - as far as I can see - never been an issue before any German court. This can be explained by two factors.

First, German law provides a very broad definition of the objectives of the corporation. This idea goes back into the early history of industrialization in the nineteenth century. The industrial revolution generated a working class which was not only materially disadvantaged but also excluded from the rapid progress of civilization. In order to reintegrate the "proletarians" into society, liberal theorists like Robert von Mohl and Lorenz von Stein taught that enterprises should be organized as cooperatives, giving voting rights and profit shares not only to investors but also to workers. In the 1920s, it became accepted by an important part of corporate management. The most important spokesman of this group was Walter Rathenau, the CEO of Allgemeine Elektrizitaets-Gesellschaft (AEG), the then major electrical company [36].
Corporate management conceived the enterprise as an institution for which the workers were as important as the investors.

In 1937, this view became enacted as Section 70 of the new stock corporation law [37]. This provision stated that "[t]he managing board is, on its own responsibility, to manage the corporation as the good of the enterprise and its retinue and the common weal of folk and realm demand" [38]. This language appeared inappropriate after 1945 so the clause was eliminated when the stock corporation law was reformed in 1965 [39]. The official explanation of the new statute, however, explicitly states that no change in the law was intended; the provision was dropped as the rule appeared evident. Today the social responsibility of the business corporation is based not only on the co-determination statutes [40] but also on the constitutional provision stating that property should be used not only in the private but also in the public interest [41].

In specifying this obligation, the courts use the notion of the "enterprise interest" [42]. It is generally assumed that it includes the interest of shareholders, creditors, employees, the local community and the public at large. It is obvious that this notion gives a lot of leeway to management. It would thus be very difficult to attack a contribution to a university in court.

Secondly, at the same time, German public corporations are reluctant to make such a contribution. Fund-raising in Germany is a hard job, much harder than in the U.S. or in Japan. All universities are State universities. Therefore, the corporations assume that higher education is the responsibility of the government and that the taxes they pay are enough of a contribution.

This is not to say that German corporations make no donations at all. There are basically three common types of donations.

One type is for specific purposes closely related to business. For example, the chemical industry gives money for chemical research in universities. Another type of donation is for specific events mostly those taking place in the local community, such as a concert, a sports event, a symposium or an exposition. In general, no large sums are involved. These donations are not based exclusively on public relations motives or the intention to be a "good citizen"; there is a co-determination factor, i.e., all or most of the employees live in the local community which benefits from the contributions. In addition, there are political donations. They involve many problems which are outside the scope of this article.

Finally, one procedural aspect would be mentioned. The big corporations in general adopt policies which are approved by the supervisory board. Within these policy parameters, the decisions will be made by the managing board. Any other donation will have to be approved by the supervisory board. Whenever more than a small sum is involved, it will not be an individual but a collective decision.
5.1.3. Mr. Shapiro's Response

Based on the facts it would be legally proper for Alpha to make the contribution; it would not be ultra vires. In fact, in a decided case relating to political donations, the Japanese Supreme Court ruled that a corporation may act in a manner which it considers to be socially responsible and of only indirect economic benefit.

It is also likely that Alpha would voluntarily make the contribution. The fact that the university is distant is not really relevant because the company may recruit employees at that university. It is not at all unusual for such gifts to be made by Japanese companies and, subject to a limitation based on a complicated formula, the contribution would be deductible for tax purposes [43].

Parenthetically, it should be noted that while philanthropy does not exist in Japan on the scale it does in the United States, nevertheless there are about 16,000 charitable corporations or trusts of which about 2,500 are national. A substantial number of these are corporate foundations to which contributions are systemically made by the corporations.

5.2. Hypothetical Number Two

Alpha is interested in purchasing a piece of land adjacent to its present property. The Chief Executive Officer of the company has undertaken the negotiation personally. He discovers that the land which the company wishes to acquire can only be purchased as part of a larger parcel which its owner is willing to sell for $6 million. The portion in which the company is interested comprises roughly two-thirds of the entire parcel. The president asks an independent appraiser to value the portion of the property in which the company is interested. The appraiser indicates that a value of $4.5 to $5 million would be a fair price. He also appears to view the other one-third of the land as of roughly the same value as the portion in which the corporation is interested.

The CEO proposes that the company buy the property in which it has indicated an interest for $4.5 million and that he and a group of colleagues together buy the balance of the parcel for $1.5 million.

Since the company's development of the land will likely increase the value of the surrounding property, the CEO also proposes to buy up surrounding property before news of the company's plans become publicly known.

What are the responsibilities of the General Counsel or any other institution or person inside the company when she learns about these proposed transactions?

5.2.1. Dean Mundheim's Response

This hypothetical deals with the duty of loyalty. Corporations provide a vehicle for aggregating wealth over indefinite periods of time. Since corpora-
tions tend to be managed by people other than the dominant investors, there is a need to insure the loyalty of the managers, to insure that the investor in the corporation will be faithfully served.

In this hypothetical, the president and his group receive an opportunity to buy land (the additional one-third parcel) at what appears to be a bargain price. Since the president is aware that the corporation is interested in buying land in the area in which the additional parcel is located, he has an obligation to present to the corporation the opportunity to make the favorable purchase. The president can take advantage of the opportunity only if the corporation has properly rejected it after all the facts have been disclosed to the corporation [44].

The opportunity can only be properly rejected by corporate decision-makers at a level of the president or higher who are not financially interested in the transaction [45]. In this case, the relevant decision-makers will be those members of the board of directors who are not part of the purchasing group and not officers subordinate to the president. Publicly held corporations in the U.S. usually have a substantial number of non-management directors on the board. The role of these non-management or outside directors is to monitor the activities of management [46]. One monitoring role will be to review transactions in which management has a conflict of interest and to assure that the conflict will be resolved favorably to the corporation.

When all the facts are presented to the directors they will have an opportunity to determine whether the corporation should buy the additional one-third of the parcel and also to determine whether the $4.5 million price for the other two-thirds of the parcel is fair to the corporation.

The second part of the hypothetical deals with the use of confidential corporate information for the personal benefit of the president. Although the law is not crystal clear [47], I think that the modern trend in U.S. corporate law would view the president's use of this information as a breach of his duty of loyalty even though it appears that the corporation will not be harmed as a consequence of purchases of land adjoining the parcel to be acquired by the corporation. If the president (or his group) make these purchases without appropriate corporate consent, the corporation could sue to recover any profits made as a consequence of the land purchases.

A particularly interesting point under American practice is raised by the question of the responsibility of the general counsel of the corporation when she learns the facts. The general counsel must advise the president that he must make full disclosure of the material facts relating to these proposed transactions to the board of directors. As I indicated previously, failure to disclose would result in a breach of the president's duty of loyalty to the corporation.

Suppose, however, the president says: "Thank you, Ms. General Counsel, for your advice. However, I do not believe that this item must be brought
before the Board and I do not plan to put it on the agenda." Indeed, the
president does not even invite the general counsel to attend the board meeting. Must the general counsel take any action? The American Bar Association's Model Rules of Professional Responsibility strongly suggests that she must [48]. Under the Rules, the general counsel's client is the corporation [49]. In a case in which an officer of the corporation is prepared to take an action or abstain from an action in breach of a duty to the corporation that could result in substantial harm to the corporation, the Rules state that the "lawyer shall proceed as is reasonably necessary in the best interest of the organization" [50]. Here it seems to me that the general counsel, having failed to get the president to reconsider his action or to inform the board, is herself obligated to inform the board because it is the next highest authority in the corporation and can be expected to act in the interest of the corporation. I think that obligation is quite clear with respect to the first part of the hypothetical, because there is a potential for substantial injury to the corporation (overpayment on the two-thirds parcel). In the second part of the hypothetical, the obligation is less clear because there is no potential for substantial injury to the corporation. However, as a practical matter I think the general counsel would feel obligated to go to the board on this issue, too. If members of the board discover that the general counsel knew the facts but did not report them, they will feel betrayed.

My point is that under developing American law, the general counsel of the corporation has a policing function and the Rules underscore that function. I do not minimize the extreme discomfort felt by the lawyer who finds that she must go over the head of the person with whom she normally deals to fulfill her obligations to the corporation. As a consequence, the general counsel will undoubtedly be very forceful in her representations to the president about the adverse consequences to him if he does not report the transactions to the board.

I should also point out that if the corporation is publicly held, there may be disclosure obligations under the federal securities laws relating to these transactions [51]. Because the general counsel will likely be involved in making those disclosures, there will be additional incentives for her to persuade the president not to breach his duty of loyalty to the corporation [52].

5.2.2. Professor Kuebler's Response

This hypothetical invites some general observations, but I should first state very briefly that the general counsel is not a clearly defined position under German law. There is no rule and not even doctrine imposing a special responsibility. The function can be performed by a member of the managing board together with other tasks such as employment relations. But it can also be carried out at the third level of the corporate hierarchy.

There are only a few cases on the issue; nearly all of them concern the small
limited liability company and not the big public corporations [53]. German law, therefore, does not have a developed and sophisticated doctrine of corporate opportunities. I would hold management liable for both transactions in the hypothetical, and I hope that the German courts would apply standards comparable to those of American law. But there are recent (unpublished) lower court decisions endorsing a much more lenient approach [54].

For the big public corporation, the legal answer to our hypothetical would be found in the employment contracts of top managers [55]. They normally have to accept the obligation to report all their private investment transactions to the Chairman of the supervisory board. In some cases they even may have to ask for a consent before they are allowed to enter into negotiations [56].

Is it conceivable that a transaction will not be reported? At least in a case like our hypothetical, this is unlikely. This is to be explained by important structural elements of the German system. Apart from the representatives of the employees, most members of the supervisory board of a big public corporation are members of the management boards of other big public corporations [57]. There are proportionately many more interlocking directors in Germany than in the U.S. An observer from abroad has referred to the Aufsichtsrat as a "device for systematic consultation between businesses whose interests are intertwined" [58].

There is a strong common interest of top management in big corporations not to rock the boat by scandals or other undesirable events. Such events may shake investor confidence, trigger legislation or provoke new co determination requests from the unions. For this reason, there are unwritten standards the violation of which may result in a broad range of sanctions. The mild penalty might be that the manager will never be promoted to Chairman nor offered a position on the supervisory board of other corporations. The severe penalty is removal. As long as the precipitating event has not been publicized, the sanction will be disguised as a resignation for reasons of bad health or important differences of opinion, much to the regret of the corporation.

5.2.3. Mr. Shapiro's Response

The CEO would be liable because the company was damaged based upon the loss of a clear opportunity to make a profit. Either the shareholders or the Board could take action to enforce this liability, from which the CEO could only be released by unanimous approval of all the shareholders [59]. In Japan, the same corporate opportunity doctrine exists as in the U.S. [60].

The practical answer would be for the CEO to suggest that the company buy all of the property and sell off the land which is not needed.

As to the surrounding property, there would appear to be no legal impediment to the CEO's purchase of this property, even though the news of the company's plans is not publicly known.

In Japanese corporations, it would not be the general counsel who would
have responsibility to act but the statutory auditor, who is elected by the shareholders and who has the responsibility to intervene in such a case [61]. The statutory auditor has the right to and does attend meetings of the board of directors [62] and is legally independent, although usually an employee of the company.

5.3. Hypothetical Number Three

Beginning roughly two years ago, Alpha’s performance has substantially deteriorated. Although the stock market has risen thirty percent over that period, the price of Alpha stock has fallen twenty-five percent. Its earnings have slipped from $5.00 a share to $2.20 a share. Part of Alpha’s problem appears to be failure of the market for its major products to expand. However, Alpha’s share of the market for these products has declined from fifteen percent to twelve percent in the last two years. There are mounting complaints that delivery of its products is slow and that its response to complaints is often non-existent. In addition, Alpha’s CEO has been arrested twice in the last six months for drunken driving, and there are rumors that he has a drinking problem.

Does anyone have a legal responsibility to take steps at this point? If no legal responsibilities compel action, what kind of action, if any, would you expect to be taken at this point?

5.3.1. Dean Mundheim’s Response

Under American law, the corporation is managed by its senior executives under the supervision of a board of directors [63]. This supervision must meet a standard of due care [64] and failure to meet that standard would subject the directors to civil liability for any harm suffered by the corporation [65]. However, even if the directors make a wrong decision, American courts are not inclined to second guess their business judgment if it is made in good faith [66]. Courts expect that the directors will take steps adequately to inform themselves about the subject with respect to which they are making a business decision [67].

Applying these general statements of the law to this situation, I expect the directors to make inquiry about the reason for the decline in corporate performance. I expect the drunken driving arrests and the rumors of the CEO’s drinking to trigger further inquiry into his fitness to continue in his job. It would be likely that, under the circumstances of this hypothetical, the directors would act to remove the chief executive officer or to force other changes. If after making inquiry, however, the directors choose to accept the variety of explanations which will undoubtedly be given for the corporation’s declining fortunes and decide not to take any further action, I doubt that the directors would be legally accountable even if the company’s fortune continues
to decline. However, the ever present threat of suit may influence the directors’ response to the corporation’s misfortunes.

In addition to the board of directors, it is likely that the long-term creditors of the corporation would take a particular interest in the poor performance of the corporation. The creditors might talk to particular members of the board and make their unhappiness known. If covenants in the loan agreements or in the trust indenture are violated, the creditors will have the option of exercising remedies under these agreements. The creditors will, however, be careful not to appear to be seeking control of the corporation because with control come certain responsibilities that the creditors probably would not want to assume.

The fall in the stock price of the corporation and the information made public because of the obligation to make full and accurate disclosure concerning the company’s financial health may serve as an invitation to a bid from another enterprise or individual who believes that he can operate Alpha’s business more effectively. This technique, known as a hostile tender offer, has become a common American response to a poorly managed enterprise [68].

5.3.2. Professor Kuebler’s Response

Diminished corporate performance is probably the case most likely to occur. With regard to drunken driving as the causative factor, all members of managing boards have their personal driver and are very much encouraged to use them for all social events in which alcohol will be consumed. An arrest would trigger enormous pressure from the other members of the managing board and the supervisory board to resign. The same would probably be true once a drinking problem has been leaked to the public. If the CEO would not agree to step down, he could be removed by the supervisory board [69]. Under German law, cause has to be shown, but the removal is effective until the courts have definitely established that there was no cause [70].

In the case that the corporate performance deteriorates, the formal responsibility resides in the supervisory board [71]. Its response would not be dictated by legal considerations to the same extent as it may be in the U.S. In fact, the timing and the form of the intervention will be at the discretion of the chairman of the supervisory board; both his personality and, more significantly his role in the corporation will guide his action. There are two models which should be distinguished:

1) In many of the manufacturing corporations, the Chairman of the supervisory board is the CEO of another corporation, possibly a bank. The amount of time he is able to spend for his monitoring task will be limited. At the same time he may be reluctant to interfere with management too early. This may be particularly true for a bank because such interference could discourage other corporations from offering similar positions of influence. Thus, the intervention may come comparatively late. That was true for AEG: significant changes in management occurred only after the crisis became obvious.
The Chairman of the supervisory board of a bank is generally the former Chairman of the managing board. In his new function he has an office in the bank, a secretary, a driver, one or even several assistants. He will go to his office every day and look into everything he thinks is important. When the managing board of Commerz-Bank had made some problematic decisions, the Chairman of the supervisory board immediately sought a majority vote to remove the Chairman and two members of the managing board. Under a special provision of the German statute, he then took over the function of the CEO for half of a year. After this interval, he hired a new Chairman of the managing board and thus was able to return to his former position. The bank was able to solve its difficulties without requesting any outside help.

In both cases it seems that neither shareholders nor creditors played an important role. Germany has not experienced any hostile takeover during the last 50 years; in this respect there is nothing of which management should be afraid. The important creditors would normally be secured. However, this may be different for the "Hausbank", the bank with which the corporation is doing most of its business. This bank will normally be represented on the supervisory board; thus its action would probably start within that body.

Both cases indicate that there may be some impact of co-determination. After AEG had gone into receivership, a British company expressed an interest in acquiring the enterprise. When the negotiations failed, it was attributed to the British company's extreme dislike of the behavior of a union representative on the supervisory board. The unions have refuted that version and indicated that there were compelling reasons to discourage the acquisition. In the case of Commerz-Bank, the stepping down of the Chairman from the supervisory to the managing board would have given the representatives of the employees the majority in the supervisory board. When the measure was discussed, their spokesperson offered that one of their members would always abstain either from attending or from voting and thus reestablish the balance. This offer was accepted and the rescue took place.

5.3.3. Mr. Shapiro's Response

Assuming there has been no illegality, the statutory auditor should report the problem at a board meeting or shareholder meeting, since the Board of Directors has the responsibility to oversee and can remove a CEO. Only the shareholders can remove a director. In practice, it would be the creditors of Alpha who would exert pressure to have the CEO removed.

As a practical matter, it would be extremely rare for a CEO of a major company to be driving his own car, much less under the influence of alcohol. Japanese laws on drunken driving are extremely strict and spot checks are frequent. As a result, a CEO generally has a car and driver at his disposal even for social occasions.
In an analogous situation involving the Mitsukoshi department store, the
CEO was removed after the company experienced financial difficulties when it
was learned that he had been giving business to a company headed by his
mistress. In a rare display of formal Board disapproval, the CEO was removed
by a vote of the directors, something which would not normally be necessary
in Japan where voluntary resignations under such circumstances are much
more the norm.

Notes

[1] This article is derived from one of three panel discussions held at the Lauder Institute of
[2] The number of Aktiengesellschaften (AG) has markedly decreased over the years with
approximately 17,000 in 1926, 2,189 in 1975, and 2,141 in 1980. 2 Business Transactions in
Germany §23.01 [2] at 23-10 n.6 (B. Ruster ed. 1985).
[3] The number of Gesellschaften mit beschränkter Haftung (GmbH) has steadily increased
from 133,182 in 1975 to 168,463 in 1977 and 255,940 by the end of 1980. Id. at 23-11.
[4] Law Concerning the Companies with Limited Liability of Apr. 20, 1892 §15, para. 3 (R.
trans. 2d ed. 1976) [hereinafter cited as AG Law]. For an analysis of the distinctions between
the organizational structure of a GmbH and an AG, see H. Jung and J. Gres, Starting
[8] Section 7, para. 1 of the 1976 Codetermination Law created a parity between stockholder and
employee representation on the supervisory board for any AG employing more than 2,000
workers and not already covered by one of the two laws applicable to the coal, steel, or iron
industries, The Mitbestimmungsgesetz of May 4, 1976. The other Codetermination Laws only
require that one-third of the membership consist of employee representatives. See The
Mitbestimmungsgesetz of May 21, 1951; The Betriebsverfassungsgesetz of Oct. 11, 1952; The
Mitbestimmungsgesetz of Aug. 7, 1956; see also E. Ercklentz, Jr., Modern German Corpora-
tion Law 103–05 (1979).
[9] The Mitbestimmungsgesetz of May 21, 1951 (the “1951 Codetermination Law”); the Betri-
ebsverfassungsgesetz of Oct. 11, 1952 (the “1952 Codetermination Law”); the Mitbestim-
mungsgesetz of Aug. 7, 1956 (the “Supplementary Codetermination Law”); and the Mitbes-
timmungsgesetz of May 4, 1976 (the “1976 Codetermination Law”).
[10] In 1868, the last Shogun, Yoshinobu Tokugawa, surrendered his political control to the
Emperor Meiji. On April 6th of the same year, the Emperor proclaimed the Charter Oath of
Five Articles setting forth fundamental policies designed to transform feudal Japan into a
modern state. Until the end of the Meiji era in 1912, the Meiji leaders created a strong and
effective government instituting many social reforms. N. Kichisaburo, The Formation of
Modern Japan 30–32 (1978). For a further introduction to the Meiji era, see P. Ch’en, The
The evolution from a French system to a German system of law took about 66 years, running from 1832 through 1898. In contrast to the Civil Code of 1890, which was based almost exclusively on French law, the Civil Code of 1898 was the culmination of the mounting influence of German law. See Takayanagi, A Century of Innovation: The Development of Japanese Law, 1868–1961, in Law in Japan 27–31 (A. von Mehren ed. 1963).

See Noda, supra note 11, at 208.

The Trust Law (Law No. 62 of 1922); The Trust Business Law (Law No. 65 of 1922).

See Noda, supra note 11, at 218–20.


Id. at 249.


The Jury Act (Law No. 50 of 1923) was promulgated in 1923, went into effect in 1928, and was suspended in 1943 by the Act to Suspend the Jury Act (Law No. 88 of 1943). Over the 15-year period that the Jury Act was in effect, there were only 484 jury cases, steadily decreasing from 143 in 1929 to 2 in 1943. Furthermore, only 12 were cases in which the defendant explicitly requested trial by jury. Urabe, A Study on Trial by Jury in Japan, in the Japanese Legal System 483–85.

Tanaka, supra note 18, at 59.

For a discussion of the two constitutions, see Takayanagi, supra note 12, at 6–15.

The Attorneys Law (Law No. 7 of 1893) created the new title – bengoshi – to replace the old term – daigennin – which carried negative connotations. This action was the result of an increased regard for the status of a lawyer. See Hattori, The Legal Profession in Japan: Its Historical Development and Present State, in Law in Japan 126–27 (A. von Mehren ed. 1963).

Advocates were requested to form associations in each judicial district in order to raise professional ethics, although governmental control was perceived as an additional reason. Hattori, supra note 22, at 118–19.

The Attorneys Law (Law No. 7 of 1893).


ALI Draft No. 2, supra note 29, §2.01(c).

Id. § 2.01(c) Comment i (suggesting that the question of reasonableness depends on an ad hoc analysis of the facts of each case).


In 1984, corporations gave 1.46% of net income to charitable organizations. These include religious, educational, and cultural groups. Council for Financial Aid to Education, 1985 Annual Survey [hereinafter cited as 1985 Survey].

See id. Corporations were the largest single source of voluntary support to higher education providing $1.57 billion or 25% of total support received.

Law of Jan. 30, 1937 §70 (The German Stock Corporation Act of 1937) [hereinafter cited as the 1937 Act].

Id. For further discussion on section 70, see Vagts, Reforming the "Modern" Corporation: Perspectives from the German, 80 Harv. L. Rev. 23, 40 (1966).

AG Law, supra note 6.

See supra note 9 and accompanying text.

Grundgesetz [66) art. 14, para. 2 (W. Ger.).


Only the part of the amount of contributions exceeding 10,000 yen may be deducted from total income, subject to the further restriction that if the amount of contributions exceeds 25% of total income, then such excess is disallowed. Y. Gomi, Guide to Japanese Taxes 1985-86, ¶ 120A, at 117 (1985).

American Law Institute, Principles of Corporate Governance: Analysis and Recommendations §§5.05(a) (Council Draft No. 8, 1986) [hereinafter cited as Council Draft No. 8].

Id. §§5.05(a) (3) (B).

See generally Committee on Corporate Laws, Section of Corporation, Banking and Business Law, American Bar Association, Corporate Director's Guidebook, 33 Bus. Law. 1591, 1619-21 (arguing that non-management directors are needed "to provide independent judgment regarding the proposals under consideration." Id. at 1619).

Council Draft No. 8, supra note 44, ¶5.04, Comment a.


Id. at Rule 1.13(a).

Id. at Rule 1.13(b).


If the general counsel participates in the drafting of disclosure documents which she knows omit required disclosures, she may be personally liable for having aided and abetted a violation of the federal securities laws.

BGHZ at 194 (GmbH-Rundschau); BGHZ at 679 (Wertpapier-Mitteilungen): BGHZ at 797 (Neue Juristische Wochenschrift); BGHZ at 43 (GmbH-Rundschau).

LG Hamburg, Mar. 1983, unpublished (Neue Heimat). Managers of this enterprise owned by German unions had done business for their own benefit in the field of their company. They were dismissed without notice, but the court upheld their employment as some members of the supervisory board had known and tolerated their behavior.

The most simple form of such a contract would contain a clause making it illegal to compete with the company. The contracts formed by big public corporations with their top managers tend to be much more detailed and sophisticated, carefully being kept confidential.

AG Law, supra note 6, ¶88, para. 1.

E. Ercklentz, Jr., supra note 8, at 110–12. The overlapping of corporate directors is subject to clearly defined limitations. See, e.g., AG Law, supra note 6, ¶100, para. 2, ¶105, para. 1.

A. Schonfield, Modern Capitalism 251 (1965).

Commercial Code (Japan) (Law No. 48 of 1899), art. 266, para. 5.

The basic test established by U.S. case law combines the "line of business" test with the "fairness" test. If the opportunity is not closely related to the existing or prospective activities of the corporation and the director's action is within the bounds of his fiduciary duty of loyalty, good faith, and fair dealing, then the director is permitted to personally take advantage of the opportunity. See, e.g., Miller v. Miller, 301 Minn. 207, 222 N.W. 2d 71 (Minn. 1974).
[61] Commercial Code (Japan) (Law No. 48 of 1899), art. 275–2.
[62] Id. at art. 260-3.
[63] ALI Draft No. 2, supra note 29, § 3.01.
[64] American Law Institute, Principles of Corporate Governance: Analysis and Recommendations § 4.01(a) (Tent. Draft No. 4, 1985) [hereinafter cited as ALI Draft No. 4].
[66] ALI Draft No. 4, supra note 64, § 4.01(c).
[67] Id. § 4.01(a) (1), (c) (2).
[68] There is a large and growing literature on tender offers. A useful starting place for research in this field is A. Fleischer, Tender Offers: Defenses, Responses, and Planning (1985).
[69] AG Law, supra note 6, § 84, para. 3.
[70] Id.
[71] Id. § 111, para. 1.
[72] Id. § 105, para. 2.
[73] Commercial Code (Japan) (Law No. 48 of 1899), art. 260-3, para. 2.
[74] Id. at art. 260.
[75] Id. at art. 257. The removal of a director must be supported by two-thirds of the shareholders present and more than one-half of the total of issued shares must be represented at the meeting. Id. at art. 343.