CODES OF GOOD GOVERNANCE WORLDWIDE *

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Abstract

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Key words: corporate governance, boards of directors, legal systems, international practices.

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Abstract

This paper examines why and how corporate governance practices are implemented across countries. We look at the worldwide development and adoption of *codes of good governance*, a set of "best practice" recommendations regarding the behavior and structure of the board of directors. We find that codes of good governance substitute for deficiencies in the legal system covering shareholders' rights. The results also show that size of capital markets, degree of government intervention, and percentage of foreign investors in the stock market are predictors of the existence of a code of corporate governance, while country openness has no significant effects. [99 words]

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I. Introduction and Overview

Corporate governance issues have recently received much attention from policy makers and from the public. Globalization processes such as the liberalization and internationalization of economies, developments in telecommunications, and the integration of capital markets, as well as transformations in the ownership structure of corporations with the growth of institutional investors, privatization processes, and increasing shareholder activism, have increased the need for efficient corporate governance practices. Such pressures for change seem to lead to the convergence of corporate governance practices (Useem, 1996; Fleming, 1998; OECD, 1998), and the consequent need for individual country agencies and actors to assess whether to introduce new corporate policies to compete in the new global corporate governance environment.

One of the central issues in the current debates of corporate control is providing the necessary disciplining mechanisms in order to make the classic principle-agent conflict of interests (Berle and Means, 1932; Jensen and Meckling, 1976) manageable. There are two manners by which countries can deal with imperfections in the protection of minority shareholders from expropriation by large shareholders and managers seeking their private interests. On the one hand, counties can reinvent their legal system to heighten shareholders' protection. This is the approach followed by transition economies (Coffee, 1999), which lacked measures for protecting private property rights. However, in general, it is not an easy proposition to change the legal system, not only because of the difficulty and lengthy process of introducing change into an exiting legal system, but also because the legal system is deeply embedded in the institutional legacies of a given country (Roe, 1994).

On the other hand, countries might take the alternative route of issuing codes of governance practices to complement the legal system, and thus correct for its imperfections. Governance codes can be linked to legally mandated disclosure requirements by stock exchanges such as in the cases of London and Toronto Stock Exchanges (Gregory, 1999), or are purely voluntary thought their compliance adds a great deal of legitimation in the eyes of investors. Corporate governance guidelines and codes are a rapid manner of filling gaps in the legal system and provide internal mechanisms for holding managers accountable and generally improving corporate governance practices, without the need of modifying the existing legal system.

In light of the former options to enhance corporate control, our working hypothesis is that countries with deficient protection of shareholders and creditors might adopt codes as a second best option to improve corporate governance practices. This research builds on the seminal work on legal systems and corporate control by La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1997, 1998, 2000) (henceforth referred to as LLSV) and La Porta, Lopez-de-Silanes, and Shleifer (1999), and contributes to it by understanding why corporate governance practices complementary to the legal system are implemented in some countries and not others.

In this paper we study the factors that determine the development and adoption of a set of similar governance practices across countries. In particular, we analyze the worldwide development and adoption of codes of good governance, a set of recommendations or “best practice” about the behavior and structure of the board of directors. Codes of good governance present a comprehensive set of norms on the role and composition of the board of directors, relationships with shareholders and top management, auditing and information disclosure, and the selection, remuneration and dismissal of directors and top managers. They are launched in response to problems of corporate performance of leading companies related to the effective board monitoring or as a consequence of institutional investors pressures to improve standards of behavior, financial reporting, and accountability of the board (OECD, 1998; Gregory, 1999). Ultimately, the codes serve to improve the overall corporate governance of corporations, especially when other corporate governance mechanisms such as takeover markets and legal environments fail to ensure adequate protection of shareholders' rights. By the end of 1999, twenty-four industrialized and developing countries had issued codes of good governance.

We examine the factors that led to the development of codes of good governance between 1988 and 1999 using LLSV (1998)'s sample of 49 countries. We find support for the hypothesis that those countries with poorer corporate governance systems are more likely to develop codes of good governance as a substitute mechanism for deficiencies in the legal system. We also test whether other factors defining the country's governance models such as type of legal system, trade openness, size of capital markets, process of government liberalization and percentage of foreign investors in the country's stock exchange might influence the issuance of new codes. We find that all factors examined, except for level of economic openness, are significant predictors of code adoption.

A parallel analysis that we conduct is identifying who the code issuers are. We find that the stock exchange was more likely to come forth the first code in common-law countries while the government was more likely to issue the first code in civil-law countries. This can be explained by the generally higher government intervention in civil law countries. Other issuers such as institutional investors, only crafted codes of good governance after professional associations did. Variance in issuers denotes differences in the enforcement of the codes. Government and stock market issuers might exert coercive pressures for the adoption of the codes of good governance, whereas codes from associations and investors might apply normative pressures.

The next section of the paper describes the antecedents and evolution of codes of good corporate governance as well as the construction of our database. Section III presents our empirical findings regarding the factors influencing the development of the codes of good governance. Section IV provides a discussion and concludes.

II. Codes of Good Governance

A. Antecedents and Evolution of the Codes of Good Governance

The first code of good governance appeared in the United States in the late 1970s in the midst of great governance ferment with business, legal, academic, and political constituencies squaring off on the role of the board. It was a transition period from the conglomerate merge movement of the 1960s (see, Chandler, 1990) to empire-building behavior by management through hostile takeovers (Blair, 1993). Early raiders such as International Nickel Company, backed by Morgan Stanley, justified the unfriendly tender offer against ESB in 1974 on the grounds that it was a financial market's mechanism to correct for ESB's bad management (Blair, 1995). In this context of charges and countercharges surrounding the takeover movement the Business Roundtable issued a Report in January 1978 entitled *The Role and Composition of the Board of Directors of the Large Publicly Owned Corporation*, which was according to Monks and Minow (1992) a response to pattern of corporate criminal behavior, and an attempt to trying to pass legislation curbing hostile takeovers. The Business Roundtable Report chaired by J. Paul Austin, CEO of Coca-Cola turned out to be a claim for the legitimacy of private power and the enforcement of accountability. The report was shifting the role of directors as merely "ornaments on a corporate Christmas tree" (Mace, 1971) to pronounced main director's duties as: (1) overseeing the management and board selection and succession; (2) reviewing the company's financial performance and allocating its funds; (3) overseeing corporate social responsibility; and (4) ensuring compliance with the law as was drafted as an attempt to improve governance capacity in U.S. corporations (Charkham, 1995).

It was not until ten years later that other countries created codes of good governance to enhance and improve efficiency in corporate governance practices. The movement underwent a rapid development in the early 1990s, particularly after the issuance of the 1992 *Cadbury Committee Report: Financial Aspects of Corporate Governance* in the United Kingdom, which took a flagship role as a deliberate test of the effectiveness of voluntary regulation and British corporate democracy (Stiles and Taylor, 1993). The British 1990 recession as well as a series of high-profile corporate failures[1], where the weakness of internal corporate control was clearly a contributing factor, raised the issue of corporate accountability both in the public mind and in the House of Commons (Monks and Minow, 1995). As it is stated paragraph 2.1 of the Cadbury Report (1992), the code was issued because of the concern at "the perceived low level of confidence both in financial reporting and in the ability of auditors to provide the safeguards which the users of the company reports sought and expected." It also emphasized the need for independent directors, larger shareholder involvement, and the establishment of audit, compensation and nomination committees (Charkham and Simpson, 1999). Moreover, sanctions were introduced to enforce that companies floated in the London Stock Exchange would comply with the Code.[2] The Cadbury Report's recommendations are highly codified allowing both companies and stakeholders to benchmark best practices, as well as to be emulated by other agencies.

Since the carving of Cadbury Report, there has been a notable rise in the number of codes of good governance. Some of the codes are the TIAA-CREF "Policy Statement on Corporate Governance" (1993), the General Motors "Board Guidelines on Significant Corporate Governance Issues" (1994), the Toronto Stock Exchange Committee on Corporate Governance in Canada (1994), and the Dutch Peters Report (1996), to mention a few.

Guidelines and codes of corporate governance are important as they provide a voluntary basis for the adoption of practices of good governance deemed essential for the establishment of corporate governance practices. Identifying the factors that influence the development of governance practices in different countries permits a better understanding of the convergence of practices and systems despite the lack of formal legal rules as well as limitations to its convergence within the globalization processes.

B. Construction of the Database

We have built a comprehensive database of codes of good governance developed worldwide until the end of 1999 to study our research question. Our main sources of information are the World Bank (2000) and the European Corporate Governance Network (2000). In order to complete and cross check information, we consulted Van den Berghe and de Ridder (1999), CAGN (1999), and Gregory (1998, 1999). For consistency reasons, our database includes only codes of good governance *per se*. We exclude laws or legal regulations, revisions and new editions of original codes, corporate disclosure codes, reports on the compliance with the codes issued, codes on the behavior of top management, consulting firm reports, codes on voting principles for investors, and individual company codes.

The countries selected are all countries identified where a code had been developed. However, we excluded "transition" and socialist countries as well as non-country issuers of codes (i.e. OECD, EBCD) in order to be able to match our data with that of LLSV (1998). By the end of 1999, 24 countries had issued codes of good governance. These countries are the following: Australia, Belgium, Brazil, Canada, France, Germany, Greece, Hong-Kong, India, Ireland, Italy, Japan, Korea, Malaysia, Mexico, Netherlands, Portugal, Singapore, South Africa, Spain, Sweden, Thailand, United Kingdom, and United States. The evolution of the codes has not been constant nor the actors involved in their development. Below we offer the evolution of the codes according to number of codes conceived by country and type of issuer.

We classify the type issuer of codes of good governance into six categories: (1) *stock exchange*, when the issuer is the stock exchange or the overseer of the stock exchange (securities and exchange commission); (2) *government*, when the issuer is the central or federal government or one of its ministries; (3) *director's association*, when the issuer is an association of directors; (4) *managers' association*, when the issuer is an association of managers; (5) *professional association*, when the issuer is an association of accounting or law professionals; and (6) *investor*, when the issuer is an institutional investor or an association of investors. Codes developed by the stock exchange in collaboration with other organizations are classified as being issued by the stock exchange. Table I presents the number of codes developed by country and by type of issuer of existing codes for the period from 1978, when the first code of good governance was developed, to 1999.

Table I

Codes of good governance worldwide

Sample of countries with codes of good governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors. Issuers of codes of good governance were classified into six types: (1) stock exchange when the issuer is the stock exchange or the overseer of the stock exchange (securities and exchange commission); (2) government when the issuer is the central or federal government or one of its ministries; (3) director's association when the issuer is an association of directors; (4) managers' association when the issuer is an association of managers; (5) professional association when the issuer is an association of accounting or law professionals; and (6) investor when the issuer is an institutional investor or an association of investors. Codes that were issued by the stock exchange in collaboration with other organizations were classified as being issued by the stock exchange. The database covers the years 1978-1999. We excluded "transition" and socialist countries (e.g. Kyrgyz Republic), codes issued by non-country entities (e.g. OECD), and revisions of codes.

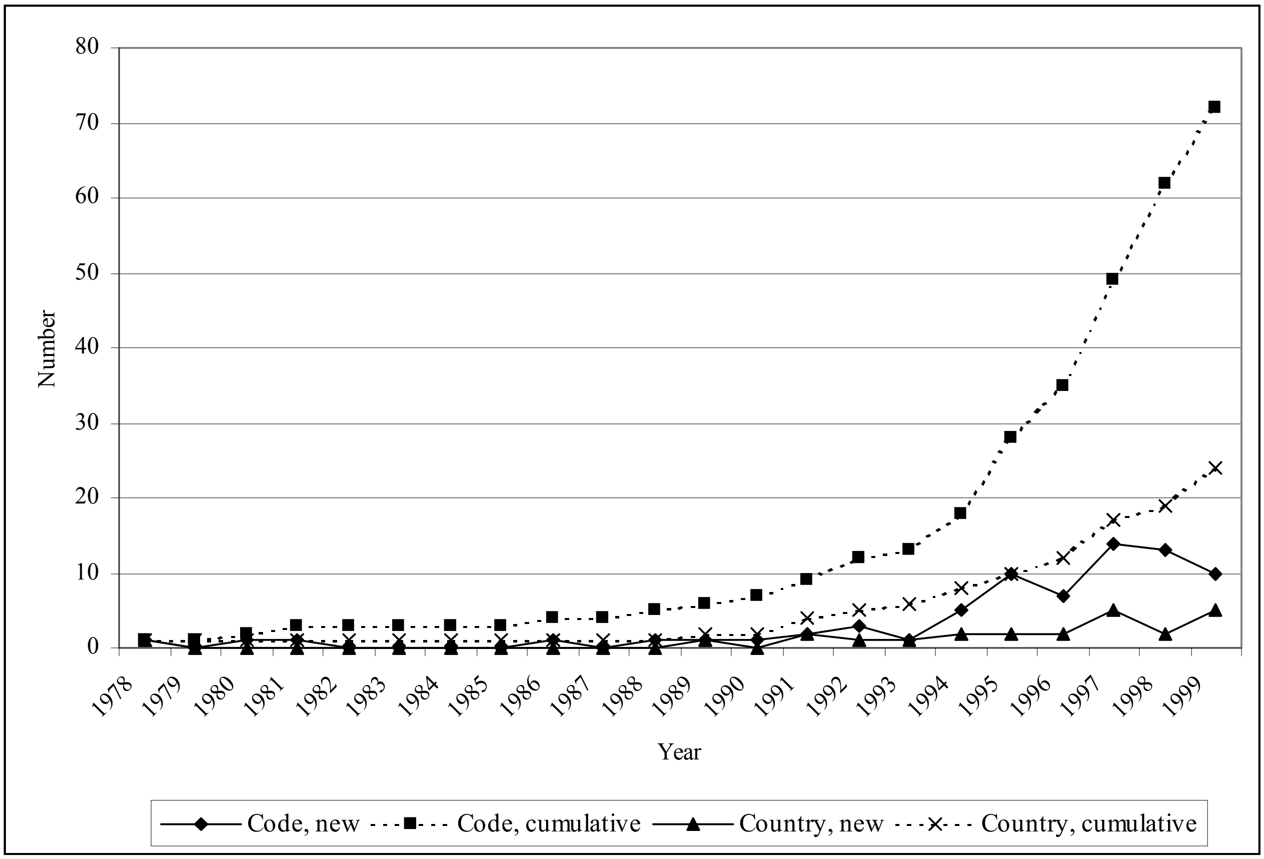
		Number of codes						Issuer of first code					
Country	Total	Stock Exchan.	Govern-ment	Director assoc.	Manager assoc.	Profess. assoc.	Investors	Stock Exchan.	Govern-ment	Director assoc.	Manager assoc.	Profess. assoc.	Investors
English-origin legal system													
Australia	4	2	0	1	0	0	1	1	0	0	0	0	0
Canada	4	1	1	0	0	1	1	0	0	0	0	0	1
Hong Kong	4	1	0	0	0	3	0	1	0	0	0	0	0
India	2	1	0	0	1	0	0	0	0	0	1	0	0
Ireland	2	0	0	0	0	0	2	0	0	0	0	0	1
Malaysia	1	0	1	0	0	0	0	0	1	0	0	0	0
Singapore	1	1	0	0	0	0	0	1	0	0	0	0	0
South Africa	1	0	0	1	0	0	0	0	0	1	0	0	0
Thailand	1	1	0	0	0	0	0	1	0	0	0	0	0
UK	11	4	0	1	0	3	3	1	0	0	0	0	0
USA	17	2	0	3	4	4	4	0	0	0	1	0	0
French-origin legal system													
Belgium	4	2	0	1	1	0	0	0	0	1	0	0	0
Brazil	1	0	0	1	0	0	0	0	0	1	0	0	0
France	4	1	0	0	2	0	1	0	0	0	1	0	0
Greece	1	1	0	0	0	0	0	1	0	0	0	0	0
Italy	2	1	1	0	0	0	0	0	1	0	0	0	0
Mexico	1	1	0	0	0	0	0	1	0	0	0	0	0
Netherlands	2	1	0	0	0	0	1	1	0	0	0	0	0
Portugal	1	1	0	0	0	0	0	1	0	0	0	0	0
Spain	2	0	1	0	1	0	0	0	0	0	1	0	0
German-origin legal system													
Germany	1	0	0	0	0	0	1	0	0	0	0	0	1
Japan	2	0	0	0	2	0	0	0	0	0	1	0	0
Korea	1	1	0	0	0	0	0	1	0	0	0	0	0
Scandinavian-origin legal system													
Sweden	2	0	0	1	0	0	1	0	0	0	1	0	0
Total													
Countries: 24	72	22	4	9	11	11	15	10	2	3	6	0	3

The evolution of the development of the codes of good governance did not follow a linear curve. Figure I shows the evolution of codes of good governance, in terms of countries and codes developed. There is a gap in the emergence of codes from the first one issued in the USA in 1978 to 1989 when "Code of Best Practice, Listing Rules" code was published in Hong Kong. After 1989, there is a continuos rise of codes that lasted until 1995. Figure I also illustrates that new codes appeared steadily throughout the early 1990s, and picked after 1995. As a result of such growth by 1995, we counted 24 countries and 72 codes of good governance.

Figure I

Evolution of codes of good governance – Countries and total number

Graph of the evolution of codes of good governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors. Country indicates the number of countries that developed a code of good governance. Code indicates the number of codes of good governance. The database covers the years 1978-1999. We excluded "transition" and socialist countries (e.g. Kyrgyz Republic), codes issued by non-country entities (e.g. OECD), and revisions of codes.

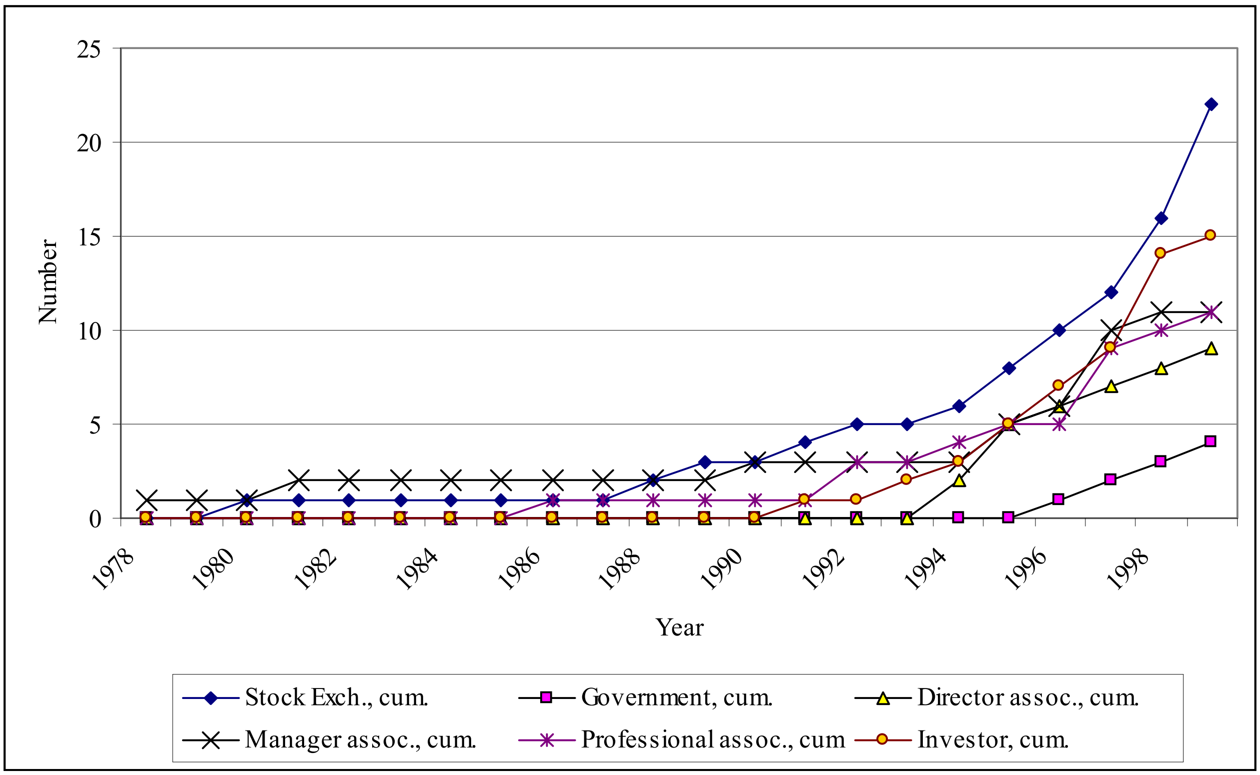


The type of issuer is another critical factor that tells us about the likelihood of enforcement and where the institutional forces originate. Figure II presents the evolution of codes of good governance by type of issuer, and proves that issuers also varied over time. Managers' associations and stock exchanges conceived the initial codes, they were then overcome by investors, professionals' associations and directors' associations which undertook a very active role. Only recently, governments issued codes of good governance.[3]

Figure II

Evolution of codes of good governance – Type of issuer of code

Graph of the evolution of codes of good governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors. Issuers of codes of good governance were classified into six types: (1) stock exchange when the issuer is the stock exchange or the overseer of the stock exchange (securities and exchange commission); (2) government when the issuer is the central or federal government or one of its ministries; (3) director's association when the issuer is an association of directors; (4) managers' association when the issuer is an association of managers; (5) professional association when the issuer is an association of accounting or law professionals; and (6) investor when the issuer is an institutional investor or an association of investors. Codes that were issued by the stock exchange in collaboration with other organizations were classified as being issued by the stock exchange. The database covers the years 1978-1999. We excluded "transition" and socialist countries (e.g. Kyrgyz Republic), codes issued by non-country entities (e.g. OECD), and revisions of codes.



The issuer of the first code of good governance in each country unveils the active role of coercive issuers. We find that first codes in a given country were produced by the stock market in 10 countries, by managers' associations in 6 countries, by directors' associations and by investors association in 3 countries respectively, and by the government in 2 countries. It is to be noted that no country had professional's associations producing the first code. Hence, the claim

Figure III

Evolution of codes of good governance – Type of issuer of code by legal system

Graph of the evolution of codes of good governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors. Issuers of codes of good governance were classified in six types: (1) stock exchange when the issuer is the stock exchange or the overseer of the stock exchange (securities and exchange commission); (2) government when the issuer is the central or federal government or one of its ministries; (3) director's association when the issuer is an association of directors; (4) managers' association when the issuer is an association of managers; (5) professional association when the issuer is an association of accounting or law professionals; and (6) investor when the issuer is an institutional investor or an association of investors. Codes that were issued by the stock exchange in collaboration with other organizations were classified as being issued by the stock exchange. The database covers the years 1978-1999. We excluded "transition" and socialist countries (e.g. Kyrgyz Republic), codes issued by non-country entities (e.g. OECD), and revisions of codes. Countries were separated into two groups based on the origin of the legal system: Common-law or English-origin legal system (Figure A) and Civil-law or French, German, and Scandinavian origin legal system (Figure B). A list of the countries in each type of legal system is provided in Table II.

Figure A. Codes of good governance in countries with a common-law legal system

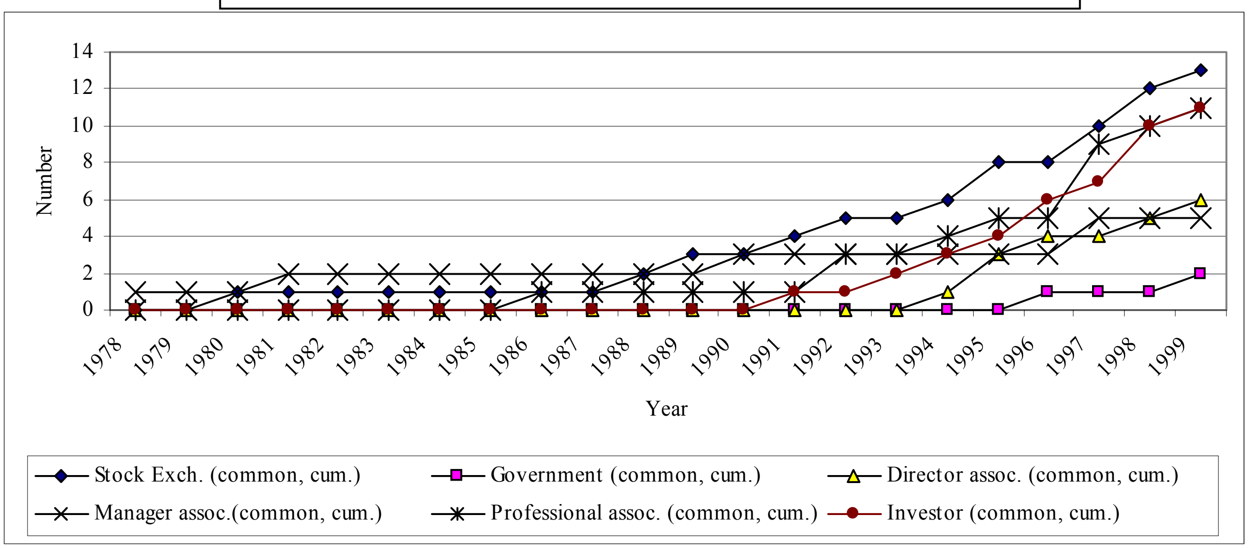
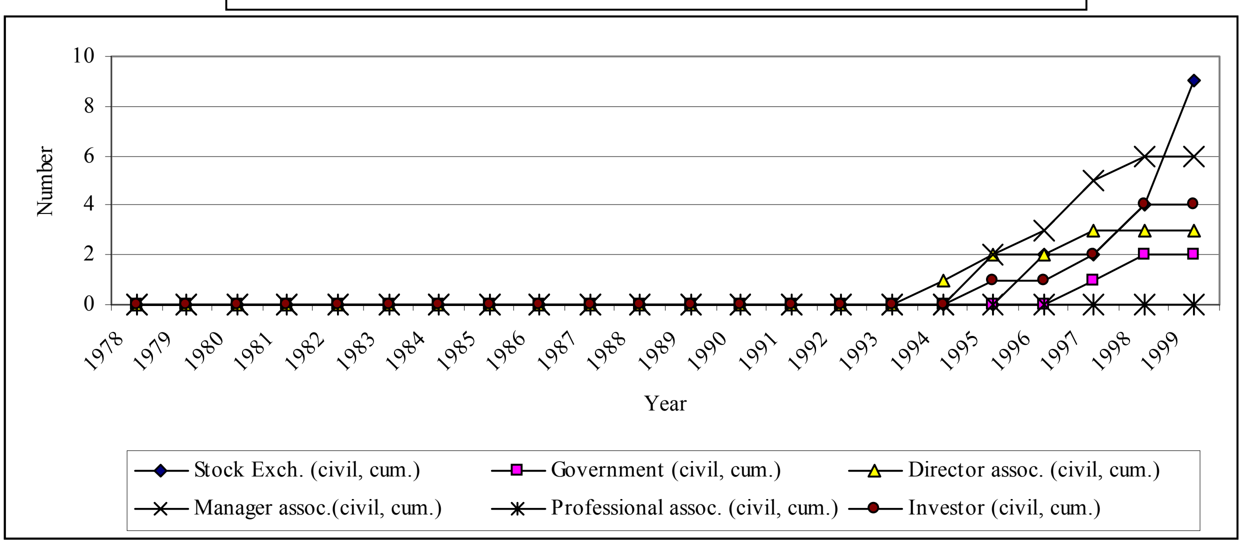


Figure B. Codes of good governance in countries with a civil-law legal system



that institutional investors were the triggers of good governance is not supported, though they might have pressured the government or the stock exchange to issue these codes. Moreover, the active role presented by managers' associations and directors' associations speaks of the view of corporate governance not only as part of the pressures exercised by shareholders, but also as part of pressures and self-regulation exercised by managers and directors.

The exploration of differences across legal systems (Reynolds and Flores, 1989) manifests different patterns of assembling codes of good governance depending on whether the countries have common-law (English-origin) or civil-law (French, German, or Scandinavian-origin) legal systems. Figure III shows the evolution of codes of good governance by type of issuer and legal system. Common-law countries experienced the origination of codes of good governance much earlier on, with the stock exchange and managers' associations being main actors as code developers. Civil-law countries created codes later, with managers' associations and directors' associations taking the lead. Thus, the legal-system seems to be a conditioning factor in the development of the codes of good governance. This idea is explored in more detail in the coming section.

III. Factors Influencing the Development of Codes of Good Governance

A. Variables

We build a systematic database for the adoption of the codes of good governance and country features to analyze the determinants of the development of codes of good governance. Forty-nine countries were included in our sample following LLSV's (1998) sample. These are countries with publicly traded companies, excluding socialist or "transition" economies. We used LLSV's (1998) sample to provide a comparison of corporate governance practices across legal systems and to employ two of their variables: common versus civil legal system, and anti-director measures contained in the country's legal system. Out of the 49 countries analyzed, 24 have issued codes of good governance.

The period of study is 1988-1999. We chose to begin our analysis in 1988 because this year is the milestone year after there was a rapid growth in countries and codes. During the period 1978-1987 only four codes were developed, and all of them were from the USA.

We codify our dependent variable, development of codes of good governance, in two different ways. The first one is a dummy variable measuring whether a country has *ever* developed a code of good governance between 1988 and 1999. The second one is a *count* variable that measures the total number of codes of good governance developed in a given country between 1988 and 1999. Only first versions of a given code were counted in the analysis.

We studied the characteristics of the country's legal system to determine whether the codes of good governance were generated as a substitute for a strong system of protection of shareholders rights or whether they were a complement to previous protections established in the legal system. Countries are classified into four legal families according to the origin of the legal system: English, French, German, and Scandinavian (Reynolds and Flores, 1989). According to LLSV (1998), countries with an English-origin or Common-law legal system provide better protection to shareholders than countries with a Civil-law legal system or French, German and Scandinavian-origin. Hence, the codes could serve to substitute for the lack of protection granted in the legal system and would be more likely to be adopted in civil-law countries.

We further investigate the protection offered to shareholders in the legal system by analyzing whether the "antidirector" measures embedded in the legal system would influence the development of codes of good governance. “Antidirector” measures calibrate whether the legal system, independently of its origin, offers protection of shareholders rights against expropriation by the board of directors. This index measure is obtained from LLSV (1998). Codes of good governance could serve as a substitute for the lack of “antidirector” measures in the legal system.

Other influencing factors in the development of codes of good governance that we studied are the causes indicated in the country codes as main reasons for the code’s creation. These causes are: globalization, privatization processes, and the rise of institutional investors. We explore whether these causes were specific to countries or whether they were part of a general trend towards convergence in corporate governance systems.

Globalization processes and the integration of the national economy in the world economy reduces the possibility of shielding inefficiencies behind barriers to trade, inefficiencies not only in the production system but also in the corporate governance system. Hence, globalization and economic openness increase the pressure for the development of corporate governance practices that will facilitate firm competitiveness by promoting transparency and accountability among directors, management and shareholders. One measure to achieve this is through the development and adoption of codes of good governance that would improve the behavior of the board of directors.

Privatization processes diminish government direct intervention in the economy and facilitate the expansion of the private sector. Privatized firms require new sets of rules on how to behave as private companies, rules that break with previous behaviors and governance structures as State-owned firms. Thus, codes of good governance can serve a guide on the appropriate behavior of the board of directors of firms where, previously, the board of directors was composed of political appointees.

The increase in the global presence of institutional investors, who search for investment opportunities worldwide, demands better governance (Hadden, 1994; Brancato, 1997). The lack of an exit option for some large investors has led to their activism and demand of good governance, not only at home, but also abroad. Active foreign investors would lead to the development of codes of good governance that will improve the behavior of the board.

We controlled for the market capitalization to account for differences in the size of capital markets, since countries with larger capital markets are more likely to develop rules and norms to improve the protection of shareholders' rights and promote effective corporate governance. Table II summarizes the variables we use and their sources.

Table II

Definition of the Variables

VARIABLE (definition)	Description
CODE (Code of good governance)	Equals one if the country developed at least one code of good corporate governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors, between 1988 and 1999, and zero otherwise. Source: Database of codes of good governance by country based on data from World Bank (2000), European Corporate Governance Network (2000), Van den Berghe and de Ridder (1999), CAGN (1999), and Gregory (1998, 1999)
CODENO (Number of codes of good governance developed)	Number of codes of good corporate governance developed between 1988 and 1999. It includes only the first issue of each code and not subsequent revisions. Source: Database of codes of good governance by country based on data from World Bank (2000), European Corporate Governance Network (2000), Van den Berghe and de Ridder (1999), CAGN (1999), and Gregory (1998, 1999)
LAWCOMM (Common-law legal system)	Dummy: 1 if the legal system is common law based (English-origin), 0 otherwise. Source: La Porta et al. (1998) based on data from Reynolds and Flores (1989)
ANTIDIR (Anti-director measures contained in the legal system)	An index aggregating shareholder rights labeled as "antidirector rights" by La Porta et al. (1998). The index is formed by adding one when: (1) the country allows shareholders to mail their proxy votes to the firm; (2) the shareholders are not required to deposit their shares prior to a General Shareholder Meeting; (3) cumulative voting or proportional representation of minorities in the board of directors is allowed; (4) and oppressed minorities mechanism is in place; (5) the minimum percentage of share capital that entitles a shareholder to call an Extraordinary Shareholders Meeting is less than or equal to 10 percent; (6) shareholders have preemptive rights that can only be waived by a shareholder vote. The index ranges from 0 to 6. Source: La Porta et al. (1998)
OPEN (Openness of the economy)	Sum of exports and imports as a percentage of gross domestic product, all expressed in millions of US dollars. Average for 1988-1998. Source: Data from World Bank

FPEGDP (Foreign portfolio investment in equity)	Inward foreign portfolio investment flow in equity as a percentage of gross domestic product, both expressed in millions of US dollars. Average for 1988-1998. Source: Data from International Financial Statistics and World Bank
GVTLIB (Government liberalization index)	Change in the indicator of governmental intervention in the economy. Equals one if the indicator dropped in value between 1988 and 1998, zero if there was no change, and minus one if the indicator increased in value between 1988 and 1998. The indicator of governmental intervention in the economy is a composite of government consumption as a percentage of gross domestic product, government ownership of businesses and industries, and economic output produced by the government. Scale from 1 to 5, with lower scores for lower levels of governmental intervention. Data for 1988 was transformed from a scale of 0 to 10 to a scale of 1 to 5 in line with data for 1998. Source: Based on data from Gwartney, Lawson and Block (1996) and Holmes, Johhson and Kirkpatrick (1997), and Johnson, Holmes and Kirkpatrick (1998, 1999)
LMKTCAP (Importance of capital markets)	Logarithm of market capitalization expressed in millions of US dollars. Average for 1988-1998. Source: International Financial Corporation (1992, 1999)

B. Results

Table III provides the means, standard deviations and correlation matrix of the variables. The correlation matrix indicates that there is a statistically significant correlation between the common-law system and antidirector measures, between the common-law system and the openness of the country as well as between antidirector measures and foreign portfolio equity investment.

Table IV presents the results from the analysis of the countries with codes of good governance. The first model performs a Probit regression using a dummy variable of the development of a code of good governance per country. The analysis reveals that the common-law legal system, governmental liberalization processes, and the market capitalization increase the probability of the development of a code of good governance. Moreover, antidirector measures in the legal system decrease the probability of the development of a code of good governance, though the latter is only statistically significant at 10%.

Table III

Summary Statistics

CODE is an indicator of the country that has developed a code of good governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors, in the period 1988-1999. CODENO is the number of codes of good governance developed in the period 1988-1999. The sample consists of the countries in La Porta et al. (1998). LAWCOMM is an indicator of the common-law legal system. ANTIDIR is an index, scored 0 to 6, of shareholders rights in the legal system that are "antidirector rights". OPEN is the sum of exports and imports divided by gross domestic product, averaged over the period 1988-1998. FPECAP is the foreign portfolio equity flows divided by market capitalization, averaged over the period 1988-1998. GVTLIB is an indicator of the changes in an index of governmental intervention in the economy in the period 1988-1998, with the value 1 indicating a reduction in intervention, a value 0 indicating no change and a value –1 indicating and increase in intervention. LMKTCAP is the logarithm of the market capitalization, averaged over the period 1988-1998. Panel A presents the summary statistics for the forty-nine countries analyzed. Panel B reports Pearson correlation coefficients. *p*-values are given in italics.

Panel A: Summary Statistics

	N	Mean	Std. Dev.	Min	Max
CODE	49	0.4897	0.5050	0	1
CODENO	49	1.3877	2.5561	0	17
LAWCOMM	49	0.3673	0.4870	0	1
ANTIDIR	49	2.4489	1.1913	0	5
OPEN	49	56.7236	49.8661	13.6666	281.8372
FPECAP	49	2.0257	4.4718	-3.8614	30.1578
GVLIB	49	0.2857	0.7637	-1	1
LMKTCP	49	4.5649	0.9291	2.1234	6.7365

Panel B: Correlation Matrix

	CODE	CODENO	LAWCOMM	ANTIDIR	OPEN	FPECAP	GVLIB
CODENO	0.5598						
	0.0000						
LAWCOMM	0.1849	0.3183					
	0.2034	*0.0258*					
ANTIDIR	0.0078	0.3316	0.6074				
	0.9577	*0.0199*	*0.0000*				
OPEN	0.2392	0.0349	0.2896	0.0755			
	0.0979	*0.8119*	*0.0436*	*0.6064*			
FPECAP	0.1594	0.1005	-0.1768	-0.3404	0.1341		
	0.2739	*0.4922*	*0.2242*	*0.0167*	*0.3581*		
GVLIB	-0.1003	-0.2927	-0.0640	-0.0523	-0.1539	-0.0096	
	0.4929	*0.0413*	*0.6622*	*0.7210*	*0.2911*	*0.9478*	
LMKTCP	0.6749	0.6395	0.0361	0.2368	0.0892	0.0647	-0.2526
	0.0000	*0.0000*	*0.8055*	*0.1014*	*0.5424*	*0.6587*	*0.0800*

The second model performs a Poisson regression of the number of codes of good governance developed in the period 1988-1999. The analysis reveals that the common-law legal system, foreign portfolio equity investment, and the market capitalization are positively related to the development of a code of good governance. Antidirector measures in the legal system are negatively related to the development of codes of good governance. The openness of the economy and processes of governmental liberalization are positively related to the development of codes of good governance, but their coefficients are not statistically significant.

Table IV

Determinants of the development of codes of good governance – Cross-country results

The model estimated in (1) is a probit regression of CODE = $\beta_0 + \beta_1$ * LAWCOMM + β_2 * ANTIDIR + β_3 * OPEN + β_4 * FPECAP + β_5 * GVTLIB + β_6 * LMKTCAP + ε. The model estimated in (2) is a Poisson regression of CODENO = $\beta_0 + \beta_1$ * LAWCOMM + β_2 * ANTIDIR + β_3 * OPEN + β_4 * FPECAP + β_5 * GVTLIB + β_6 * LMKTCAP + ε. The sample consists of the countries in La Porta et al. (1998). The dependent variable CODE is an indicator of the country that has developed a code of good governance, a set of recommendations or "best practice' about the structure and behavior of the board of directors in the period 1988-1999. The dependent variable CODENO is the number of codes of good governance developed in the period 1988-1999. LAWCOMM is an indicator of the common-law legal system. ANTIDIR is an index, scored 0 to 6, of shareholders rights in the legal system that are "antidirector rights". OPEN is the sum of exports and imports divided by gross domestic product, averaged over the period 1988-1998. FPECAP is the foreign portfolio equity flows divided by market capitalization, averaged over the period 1988-1998. GVTLIB is an indicator of the changes in an index of governmental intervention in the economy in the period 1988-1998, with the value 1 indicating a reduction in intervention, a value 0 indicating no change and a value –1 indicating and increase in intervention. LMKTCAP is the logarithm of the market capitalization, averaged over the period 1988-1998. White's heteroskedasticity-consistent standard errors are given in parentheses.

	(1)	(2)
INTERCEPT	-11.5764 ***	-8.0130 ***
	(2.4184)	(1.0922)
LAWCOMM	2.2633 ***	1.5100 ***
	(0.8068)	(0.3857)
ANTIDIR	-0.8298 *	-0.2859 **
	(0.4908)	(0.1342)
OPEN	0.0039	0.0010
	(0.0054)	(0.0016)
FPECAP	0.1745	0.0475 ***
	(0.1461)	(0.0133)
GVTLIB	0.9172 **	0.1110
	(0.4484)	(0.2366)
LMKTCAP	2.6025 ***	1.5875 ***
	(0.6014)	(0.1887)
Loglikelihood	-11.8652	-47.2714
Wald Chi2 (6)	33.93 ***	196.61 ***
Number of observations	49	49

***, **, and * indicate statistical significance at 1, 5, and 10 percent, respectively

Our results suggest that codes of good governance complement shareholders' legal protection in already strong legal systems such as the common-law system. However, it is very interesting to note that codes also substitute for deficiencies in the legal system by being originated in countries with fewer antidirector measures in the law. Therefore, codes of good governance support the protection of shareholder rights, reinforcing the legal protection and substituting for its deficiencies.

The results also support our hypotheses that as globalization processes continue, there would be a greater development of codes of good governance. In addition, government interventions in the liberalization of their economies and opening to international trade, as well as, the international spread of investors, launch the incentives for the development of codes of good governance and the spread of corporate governance practices worldwide.

IV. Discussion and Conclusion

This paper analyzes the factors that determine the emergence of similar corporate governance practices in 49 countries around the world. In particular, we study the development of codes of good governance, a set of recommendations or "best practice" about the behavior and structure of the board of directors. This practice has become central to corporate governance debates, particularly regarding its institutional impact on international management practices and the need for public policy adjustments to the new forms of shareholder activism.

The most relevant finding is the confirmation of the hypothesis that codes of good governance serve to improve country-level corporate governance by substituting for deficiencies in the legal system. In particular, we show that countries with legal systems with imperfect protection of minority shareholders from expropriation by large shareholders and managers seeking their private interests, that is, countries with low "anti-director" measures, are more likely to develop a code of good governance. Moreover, we discover that when differentiating between the two main legal systems, civil and common law, countries in the latter tradition are more likely to develop a code. Other factors that determined code development are the importance of capital markets, processes of governmental liberalization, and the weight of foreign investors in the stock exchange. These are factors that reflect not only the need for improving corporate governance practices, but also the incentive to do so. The openness of the economy did not have a significant effect in the likelihood to develop a code.

This is an important first cut in the examination of the factors influencing the development of new corporate practices around the world, and a test as well as extension on the work of LLSV (1997, 1998, 2000) and La Porta, Lopez-de-Silanes and Shleifer (1999) on corporate governance and control across countries. Future studies will follow three related avenues. One will analyze the timing in the adoption of corporate governance codes and the role of foreign investors in the diffusion of such practices. Another will study differences in the content of the codes and explain why countries develop similar or different codes, relating their content to the nature of the protection offered to investors in the legal system. The final line of study will analyze the impact of the heightened protection of shareholders by the codes and the influence of their development on the investment in firms and economies.

V. References

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VI. Endnotes

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[1] According to Monks and Minow (1995) the most notable corporate failures where the collapse of Asil Nadir's Polly Peck International, Robert Maxwell's MGN/Pergamon empire, and the Bank of Credit and Commerce International," p. 303. For instance, it was discovered that Robert Maxwell had stolen $700 million from his employees' pension fund.

[2] According to Charkham (1995), "The Cadbury Report recommends that listed companies in respect of accounting years ending after 30 June 1993 should state in the report and accounts whether they comply with the Code and identify and give reasons for any areas of non-compliance," p. 271.

[3] When referring at the government as a type of issuer, we have to take into account that the database does not cover changes in the legal system, as it was the case in Germany and Italy, for example.