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Corporate Governance and Corporate Finance: A Cross-Country Analysis

Marina A. Burmistrova

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Abstract

This paper presents a review of the modern tendencies in corporate governance and legislation in Russia. First, by focusing on the American and German models, the paper tries to establish the ideal analytical model of corporate governance against which one can then compare the existing body of corporate legislation in Russia. In developing this comparative analysis, we explicitly account for some key historic drivers of corporate growth which strongly influenced the development path of national corporate governance systems. We demonstrate that the prevailing way of corporate financing, its historical background, and the convergence of national legislation due to of the economic globalization are among the key factors to consider. We also show that behind the signs of economic growth triggered by the positive macroeconomic fundamentals and sky-high government oil revenues, one can also discern persistent signs of economic weaknesses in the Russian financial sector. The banking sector and the national stock market remain by and large underdeveloped and overregulated. Both are highly volatile, mainly due to their large dependence on international capital flows and the excessive government regulation. The Russian model of corporate finance is neither "debt-based" nor "equity finance based" as the government budget and retained earnings still remain the key sources of corporate financing. The government's role as a key financier of corporate development only adds to the increasing influence of the government on private business. The brunt of government regulation however is borne by largest Russian companies. Smaller corporations, most of which are tightly held closed private companies, are left out of the government regulatory net. The "top-down" approach to corporate governance actively pursued by the state often translates into problems with the quality of government regulations and difficulties with their practical implementation.

Similar to the German corporate law, the Russian corporate legislation has chosen the "ex ante" way of regulation, aimed at preventing potential violations of shareholders' rights. This highly rigid approach was chosen in the early 1990s as a response to the rising tide of violations of fundamental principles of corporate governance which at that time could not be dealt with by the undeveloped system of commercial courts. On our opinion, the best system of corporate legislation Russia can have is the one that relies on best corporate practices and provides enough legislative flexibility for catering to real legislative concerns of various categories of companies. The current Russian legislation gravely suffers from the lack of flexibility which has become the result of the government "top-down" approach to regulate the corporate relations by imperative legislative norms. In the absence of a major regulatory reform or changes in the prevailing mode of corporate financing, corporate governance, although in its current highly prescriptive form, is likely to remain the topic of concern for only few large listed companies.

Key Words: Corporate governance, corporate finance, corporate legislation, Russia

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1. Introduction

In this article corporate governance is viewed as the system of economic and legal institutions that defines the relationships existing between corporate legal entities such as public and private limited liabilities companies, their investors, and the government regulatory bodies. This definition is similar to the definition of corporate governance, given by Cadbury (1999:1)[1], and goes well beyond the issues of control and management, which are the focus of the definition given by the Organization for Economic Co-operation and Development (1999:1)[2]. The ongoing academic discourse over corporate governance has a long history. Most of debate however focuses on the models of corporate governance in different countries and the ways of their future development. Some scholars take a position that corporate governance has always been the extension of government policy towards the financial and corporate sectors. For example, in the USA, the fear of a new banking crisis after the Great Depression led to the enactment of a highly restrictive banking legislation which prohibited banks from combining commercial and investment activities (dos Santos, 1996:1), having branches in several different states, and providing certain financial services across the country. But a US style corporation today is more a local custom than the result on an inevitable economic evolution (Roe, 1993:1936). Nevertheless, the US corporate sector is a phenomena worth studying as it is perhaps the only well developed corporate financing model that relies almost exclusively on small private investors, which to the astonishment of many critics, have turned the US corporations into the most highly capitalized companies in the world. Today, even the largest international banks will find it hard to master enough financial resources for acquiring any significant minority stake in the US Fortune-1000 companies. This so-called "Anglo-Saxon model" is unimaginable without a well-developed stock market, as it aims to

[1] Corporate governance is holding the balance between economic and social goals and between individual and communal goals. The aim is to align as nearly as possible the interests of individuals, corporations and society. The incentive to corporations is to achieve their corporate aims and to attract investment. The incentive for states is to strengthen their economies and discourage fraud and mismanagement.

[2] Corporate governance is the system by which business corporations are directed and controlled. It specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders and provides the means of attaining those objectives and monitoring performance.

attract external investment in companies' stock from many small (naïve and passive) investors. These investors tend to have little influence over the companies' fortune and thus are primarily concerned about the quality of financial disclosure and other rules to protect their investment interest. In response to these popular demands, the "Anglo-Saxon" model creates a system of checks and balances to protect the interests of shareholders by clearly defining the authority and responsibilities of management, requiring adequate financial disclosure, protection of shareholders' rights, including minority shareholders, and limiting the interference of the state and other third parties in corporate affairs.

The "Anglo-Saxon model" of corporate governance however has not been universally accepted world-wide. The German corporate governance system illustrates an alternative mode of corporate development, which mainly relies on large institutional investors (such as banks) and is characterized by relatively undeveloped capital markets. In this system, the interests of society and the state are of great importance and have precedence over individual property rights, which in comparison with the Anglo-Saxon Model are restricted. Banks, creditors, employee trade unions and professional associations play an important role in corporate life; banks are allowed to invest and actively participate in managing companies as one of the main shareholders. The main reason behind such a model has been a fear of consolidated corporate control that could translate into a strong influence of corporate interests on the state policy (Pistor 1999:6). Hence, the German society has adopted a system of corporate legislation which protects all stakeholders, not only the shareholders, through special norms on co-determination and employee guaranties.

Although nations are free to choose how to develop their economies and which models of corporate development fit their interests best, according to the theory of path-dependence they may not be entirely free (Bebchik, Roe, 1999:130).The theory maintains that the historical structure of the financial and real sectors defines the way these sectors will develop in the future, and, consequently, the prevalent model of corporate governance. Buck and Shahrim (Buck, Shahrim, 2005:44) provides interesting examples of government policy failures to build country corporate development models without considering the past and the national culture. After the

World War II, for instance, the US occupation authorities in Germany and Japan attempted to dissolve enterprise cross-ownership in Japan and dismantle family and bank networks in Germany by introducing the US-style stock market capitalism. These attempts failed however and by 1970 large industrial and financial cross-holdings were again the order of the day in both counties. Japan also presents a very special case, where the US model of stock market and corporate regulation co-exists with concentrated ownership and wide corporate cross-holdings.

The understanding of the principal drivers defining the nature of modern corporate governance systems is crucial for the analysis of their future possible development. Without taking sides in the pertinent academic debate on what constitutes the key drivers of corporate governance systems, we can only accept they are likely to include the economic factors, government policy, and the historical development path of the corporate sector.

2. The US vs. the German Corporate Legislation Models: What Works Best?

Let us now consider the principal legislative mechanisms constituting the foundation of two opposite models. As a basis for our comparison we will use the classification, used by La Porta et al. in their paper "Corporate Ownership Around the World" (La Porta et al., 1999:508). He distinguishes between two types of economic systems – a "bank-centered" and a "market-centered". Investors in a "market centered" financial system rely more on equity finance, which has several specific characteristics. Firstly, shareholders are entitled to manage a corporation and receive profits. Secondly, shareholders' claims to the company's value are residual, meaning that their claims would be satisfied only after those of creditors in case of insolvency. Although sometimes shareholders can legitimately claim back the money invested in a firm (appraisal rights), this is more of an exception from the general rule. To manage their investment profitably and efficiently, investors must have the ability to broadly diversify their portfolios and quickly move in out of investments at a minor transaction cost.

This, in turn, requires a rather well developed system of national legislation on shareholders protection.

The US corporate governance model differs from the others by the dominance of market institutions, such as rating agencies, investment analyst reviews, and adequate financial disclosure ensured by the universal acceptance of the GAAP (Generally Accepted Accounting Principles) in financial reporting of the US companies. In general, the US corporate legislation can be characterized by the high level of flexibility that creates wide open opportunities for companies in the areas that are not explicitly prohibited by law. The US legislation, for instance, does not require closed companies to disclose their financial statements, but, at the same time, to ensure adequate protection of small portfolio investors, which in the US constitute the majority of companies' shareholders, public corporations are the most regulated in the US. The well functioning system of shareholders' protection in the US relies on the fiduciary duties doctrine and high professionalism of the courts.

At the first glance, the most famous corporate code in the USA, the Delaware corporate law, is rather weak in protecting shareholders. The management has wide discretion in making the most important corporate decisions, like mergers and acquisitions, and use of anti-takeover protective mechanisms such as capital dilution or other "poison-pill" approaches (Pistor et al., 2002:816). The US is one of few jurisdictions, which empowers corporate boards to block hostile bids. In the US, a general shareholders meeting can only ratify critical corporate decisions, but cannot initiate them.

What makes the system work however is the consistent application by the courts of the principles of the fiduciary duties. While the doctrine of fiduciary duties is also used in many other countries, it has a rather special distinct meaning the US legal practice. The doctrine of fiduciary duties can be equally applied to the companies' directors, auditors, shareholders, and creditors. For instance, as has been demonstrated by the US court practice, corporate boards are not obligated to implement the decisions of shareholders' meetings if these decisions may adversely affect the interests of the minority shareholders (Unocal Corporation v. Mesa Petroleum Co, 1985:1). The duties of the directors include even the protection of the

company against its own shareholders. Pistor and Xu (2003:78) call the US law "enabling", because the primary role of the court is to fill the gaps in the existing legislation rather than regulating by prescriptive norms. The ability of the US courts to fill in the legislative gaps through residual law making and retroactive law enforcement functions ensures the successful implementation of the fiduciary duties principle.

Corporate owners in the economies relying on debt finance need not to sell their equity in order to raise the funds. Instead, they can rely on debt. Their creditors however would have the claim of first order to the company and may want the shareholders to guarantee their debt. Shareholders' equity capital plays the role of this guarantee, which explains why the obligatory minimum capital requirements exist in most European countries. As a result, after having incurred the capital costs to support the guarantee, the European companies are less eager than their US cousins to seek corporate financing from the stock market, and instead prefer to rely on borrowings from banks. This trend can be illustrated by the meager number of Initial Public Offerings (IPOs) in Germany over the last years 20-30 per year. Yet, the European companies are more likely to use equity market financing in cases of financing corporate consolidations, mergers, and acquisitions.

The concept of fiduciary duties is not foreign to the German law as well. In Germany, the corporate board represents not only shareholders, but also employees, and creditors. The law states that managers should be diligent entrepreneurs, and that they must not compete against their own company. But the legislation does not spell out the mechanisms for pursuing legal action, and sets the threshold of shareholders' ownership that entitles them to such actions at 5% of company's stock or 500,000 euros. A legal action against a manager found in violation of this requirement can be filed by the supervisory board, but in reality this is rarely the case since it would imply that the supervisory board has also breached its duties. Better developed is the application of the fiduciary duties doctrine to issues arising between shareholders. The court practice has some cases, when major shareholders were found liable for negotiating with the board the deals, which were not in the interest of minor shareholders. The directors are personally liable to creditors if acted negligently, but negligence is very difficult to prove (Baums, Kenneth, 2003:14). Under the German

legal system, at the first glance, shareholders appear to have a broad spectrum of rights: they can call a shareholders' meeting and decide how to distribute earnings, or appoint auditors, or even instruct the management through the so called "direct voting" procedure on the course of corporate actions. But their rights are significantly limited by the "co-determination rules." In general, the German law is the opposite of the US corporate law model – as the whole system of legislation relies on the detailed provisions of the law, aimed at preventing potential failures of corporate governance at the company level. As a result, some of the fiduciary duties, such as information disclosure, notifications about shareholders' meetings, conflict of interest provisions are codified. One can observe that the US and the German legal models provide two different ways of legislative regulation and law enforcement which to a large extent can be explained by the way the corporate sector is financed in each respective country.

3. Convergence of Two Corporate Models: Is It Really Happening?

The last few decades witnessed the globalization of the world economy and a gradual convergence of national legislations. The emergence of the pan-European unified economic and legal zone gave a new impetus to the ongoing scholarly debate about the convergence of the Anglo-Saxon and Continental Models. Is the convergence really taking place? To a large extent, we think it is the case. The latest European Union Directives, for instance, take into consideration the British legal practice and corporate law on takeovers, reorganizations, and stock market regulation, which have already strongly influenced the current corporate legislation of the Continental Europe. To illustrate this observation, we can point to the current debate about the necessity of removing from the European corporate legislation the requirements of the minimum capital and obligatory nominal shares, as well as the importance of including in the EU Directives the provisions on "squeeze-outs", which were previously considered foreign

to the Continental legislative norms. As stated in Sir Winter Report,[3] the vast majority of the respondents agreed that the minimum capital requirements do not guarantee any meaningful protection to creditors. The report provides a remarkable evidence of how academic views have changed since the implementation the EU legislation.

Over the last decade we could also see the emergence of worldwide global financial institutions capable to provide a full spectrum of financial services (from banking to investment management and insurance), concentration of property and corporate control in the US, and an ever increasing role of large foreign investors (usually from the Anglo-Saxon jurisdictions), which expect the European companies to comply with their standards of corporate governance.

We must also point out however that some scholars maintain the view that convergence is still not so significant and that the changes in ownership structure have not been universal (Roe, 1993:1958). While legislative changes are important, they should be viewed in a larger context of the historical background and the national specificity of corporate governance systems. For example, in the US, even though institutional investors own about a half of equity in NYSE-listed companies, their individual holdings usually amount to a small percentage of a given company's capital, so coordination among a substantial number of such investors would be required to ensure proper monitoring of management's performance and agreement on the overall objectives of corporate development. Such coordination would not be easy to achieve by regulatory means alone.

Although it is still too early to draw any serious conclusions about the acceptance of the new European legislation in the Continental Europe, it is already clear that this process is not and will not be so easy. One can already observe strong opposition in Germany and the Netherlands to the EU initiatives on deposit insurance, freedom of establishment jurisdiction rules, disclosure of Chief Executive Officers' remuneration packages, cross-border corporate takeovers in Germany, and co-determination rights (Centros v Erhvervs-og Selskabsstyrelsen, 1999:1; Überseering et al., 2002, Mobilcom , 2003:1).

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[3] Report of the High Level Group of Company Law Experts on a Modern regulatory Framework for Company Law in Europe, 2002: 78.

4. Choosing Between the US and Continental Europe Models: What Would Work Best in Russia?

While answers to this question are likely to vary a great deal, one cannot go wrong by suggesting that it is some sort of combination of both corporate governance models that would work best in Russia for the very simple reason that features of both systems are already present there. Before considering what hybrid corporate governance system would be best suited for the needs of the Russian corporate sector, let us first examine how it was formed.

Market reforms in Russia were carried out by means of voucher privatization, which, according to the reformist ideas of the international financial institutions (Ellerman,2002:3), should have led to the emergence of a class of small proprietors, actively engaged in stock market mechanisms. However, the reality is rather different. In 1996, the Federal Law on the Regulation of Stock Market was adopted, which incorporated many provisions from the Anglo-Saxon corporate legislation, effectively creating a US style system of stock market regulation. However, this approach did not consider the fact that the newly born Russian market economy was being built on the still smoldering foundations of the Soviet centrally planned economy. For many years, the main goal of Soviet enterprises was the fulfillment of planned indicators, a far cry from the textbook model of corporate profitability and efficiency. As a result of privatization, a great number of formerly state-owned enterprises faced the necessity to reorganize production process and to get rid of unprofitable and non-core assets.

Under these circumstances, often with negative market valuation and non-existent profitability, such companies could not be of interest to small investors, which from the outset, made the Russian stock market an unlikely mechanism for promoting the US style widely spread corporate ownership. In the absence of interest on the part of small investors in financing the newly privatized Russian companies, which was perpetuated by the absence of developed legislation on protection of minority shareholders, the companies had no choice but to turn first to self-financing through reconstruction of the Soviet era economic ties, and then to large private equity investors. The latter proved to be the main source of corporate financing in the 1990s

due to the very attractive valuation of prime corporate assets during the privatization, and the cultural preferences for concentration of ownership and control in the hands of few largest shareholders. Many empirical studies conducted in 1999-2001 by the Higher School of Economics (HSE), the Bureau of Economic Analysis and other organizations (Dolgopyatova, 2004:22), show that the average percentage of corporate ownership for the first wave of Russian shareholders varied from 28 to 42% depending on the characteristics of the company. Consequently, the government policy aimed at the implementation of the Anglo-Saxon corporate model in Russia was doomed to a failure already at the initial stage of reforms, since it was at odds with the objectives and the financial circumstances of most Russian companies. At that stage of corporate development, to successfully emerge from their financial distress, the Russian companies needed to find one large proprietor. The ensued concentration of ownership at the end of 1990s, has created favorable conditions for the economic growth achieved after 2000.

The end of 1990s witnessed major changes in the global economic environment brought about first by the Asian economic crisis and then by the 1998 depreciation of the ruble, with a subsequent Russia's debt default. The election of president Putin in 2000 entailed the implementation of liberal, but at the same time very strict socio-economic program that resulted in a major tax reform, and elimination of government budget deficit and non-payments problems. The cornerstone legislation on "On Joint-stock Companies", "On Limited Companies", "On Stock Market" was enacted at that time. All these developments translated into the improved macroeconomic fundamentals and helped to raise the level of competitiveness of the Russian companies in the world markets, and attract more foreign investment to the country. These events also initiated new tendencies in the development of the Russian corporate sector.

On the one hand, during the 2000–2003 period one can observe the continuing concentration of corporate ownership. During this period the largest in the history of Russia corporate mergers and acquisitions were announced such as the BP - TNK merger . On the other hand, the increased interest of foreign investors in the Russian companies and the policy of international expansion pursued by the largest Russian

companies have finally created the environment conducive for the development of modern institutions of corporate governance that could considerably increase the investment attractiveness and thus the valuations of Russian enterprises. During 2000-2003, one can also observe the first issues of American Depositary Receipts in foreign markets by the largest Russian companies, and the increased corporate interest in such financial instruments as corporate bonds.

Just like it was the case in the post-war Japan or Germany, one can observe that the development of Russian corporate sector was strongly influenced by the highly concentrated ownership structure patterns inherent to the Soviet economy, which prevailed at the end despite the adoption of the US-style corporate legislation. This confirms the main postulates of the path-dependence theory and its applicability in Russia.

5. The Main Characteristics of the Russian Corporate Sector and How They Affected the Choice of the Corporate Governance Model.

Let us now take a more detailed look at the Russian corporate sector and its underlying incentives. The largest part of the Russian corporate sector consists of the so-called “closed" companies such as LLCs, “closed" JSCs, and even open" JSCs, which are more similar to closed companies by their economic nature. According to the economic statistics, by the end of 2003, there were only 200 listed companies in Russia. Besides the fact that the companies by and large preferred bond financing over equity, the statistics also reveal a very limited number of initial public offerings (IPOs) that took place over the last few years and that the stock market remains largely undeveloped. But in Russia, in contrast to Germany, the undeveloped stock market is not compensated by the existence of a strong banking sector. The former Soviet savings bank “Sberbank” still retains the dominant position in all segments of the consumer banking market. Commercial banks are usually the “pocket" banks of large industrial holdings that do not engage in any significant lending to outside companies. The current banking regulations restrict banks’ ability to offer a large

spectrum of financial services such as mortgage finance, securitization, investment management, and insurance. The Russian legislation contains plenty of restrictions impairing the development of the financial services industry such as currency controls, licensing, non recognition of transfers of future receivables, restricions on money pledging and other collaterization techniques which are often used in debt financing in the developed markets.

In the first quarter of 2004, the Russian stock exchange index increased by 33 % (Strategy of development of financial markets, 2005:70). Most of the gains however were lost at a later stage, with the index finishing the year only 8,3% higher, which was the minimum growth rate for the whole period of 2000-2004. The first quarter of 2005 however was more successful. The main indexes have shown significant growth (MICEX - 8,3%, RTS - 8,95%. As a result, the growth for the first quarter of 2005 was more significant, than for the whole 2004 year. Behind these statistics, however, some negative trends can be descended. The investment figures show that in 2004 the total amount of capital raised by Russian companies was on the order of USD 15.5 billion, the largest part of which – USD10. 2 billion came from abroad. The main way of raising the funds were borrowings and IPOs on foreign stock exchanges. That means, that the largest Russian companies do not view the national stock market as a worthwhile mechanism for raising capital. In total, 75% of all transactions in Russian securities were made outside the country, which at least partially can be explained by the excessive regulation of registration of stock issues (Kostikov et al., 2005:3).

Due to the high volume of transactions originated outside the country, the Russian market generally follows the dynamic of international stock markets, and is strongly influenced by economic events outside the country. The main source of foreign investments is the money, that had been transferred abroad earlier rather than new direct foreign investments. In 2004, capital raised at the Russian stock exchange accounted for only 19, 6 % of the total value of corporate financing. It is ironic that almost 15 years since the collapse of the centrally planned economy and the creation of new market institutions, the government budget still accounts for the second largest share of corporate financing (16,2%), being only superceded by corporate retained

earnings (around 25-28% over the last 2 years) according to data of Bank of Russia (2004). Since the local stock market does not play an important role in corporate financing, its role as a setter of corporate governance standards is limited. Companies' interest in the stock market is mainly explained by their interest in corporate image building.

The "top-down" introduction of the Russian corporate governance model has brought not only positive outcomes for the Russian corporations such as the popularization of the idea of good corporate "behavior", which resulted in the enactment of the Corporate Behavior Code in 2001, but also some negative ones. A major push for corporate transparency and improved regulation of the securities exchange was frequently used by the state regulatory bodies as a pretext for expanding their regulatory authority. Such an aspiration of the state agencies for a larger control of the market led to the increasing transaction costs for companies.

While corporate governance is more and more becoming the topic of the day for Russian companies, according the data supplied by International Finance Corporation Independent Directors Association,[4] the corporate governance standards so far have been adopted only by the limited number of companies. The standards cover such issues as information disclosure, Board of Director's competence, handling of shareholder's meeting issues, and internal controls. According to the IFC and IDA data, only 47 % of Russian companies are familiar with the basic provisions of the Code of Corporate Governance and only one third of them adopted recommendations in practice. These studies covered 307 companies with more than 50 shareholders located in the four largest regions of the Russian Federation.

The Russian companies vary greatly in terms of their size, economic behavior, business history, and legal organization. The latter can be quite important as the economic motivation of "Open" and "Closed" companies is different. The former are likely to be outward oriented, frequently looking beyond the Russian market, and are eager to attract large foreign investors to finance their growth. In order to achieve their economic objectives they need reliable legal protection of property rights to preserve assets acquired since the beginning of the transition period. For "Open" companies

[4] Survey of Corporate Governance Practices in Russia's Regions, 2003:16.

plans' to raise capital outside of Russia, corporate governance is viewed as an important element of the strategy to increase their market valuation and investment attractiveness. In response to the demands of "open" companies, the Russian standards of corporate governance for publicly listed companies are already well developed and are similar to the standards of OECD countries set out by the German code of corporate governance (OECD, 1999).

The "Closed" companies have a completely different set of objectives. They are likely to be focused on minimizing their operational costs, protecting themselves from outside interference, and trying to free up additional capital through internal restructurings. For this type of companies corporate governance is of little importance due to the already high concentration of ownership in the hands of internal private equity investors and management, which gives them the needed level of corporate control.

However, the level of overall compliance with these principles even in case of "open companies" is another matter. According to the research, published by the Russian Association of Corporate Directors, the Russian practice of corporate governance has several weaknesses. The Russian business leaders often disclose even more information, than their foreign counterparts, but this information suffers from the lack of standardization and is typically of low quality. The research indicates that there is no visible correlation between the level of financial disclosure and corporate governance standards adopted by a company on the one hand and its valuation in the Russian stock market on the other hand (with a few notable exceptions such as Yukos in the past). Russia still suffers from the lack of legislation on personal management responsibility, absent disclosure requirements for the company's ownership structure, and the lack of legislation on insider trading and affiliated persons. The fiduciary duties doctrine has been incorporated in the corporate law, but the court practice in this area is very poor. There is no real legal protection against "black mail" and scarce regulation on corporate takeovers.

The corporate legislation in Russia followed the preventive, "ex-ante" model of regulation. Similar to the European legal system, the company law provides many detailed rules, which specify every aspect of organization of shareholder's meetings,

the rights and obligations of directors and shareholders, and creditor's rights during reorganization. The Russian Joint Stock Corporation Act is also unique compared to all other jurisdictions, as it stipulates the obligatory cumulative voting. The LLC law however is too rigid in its prescriptive provisions to ensure the successful development of companies. The law gives shareholders non-conditional appraisal rights, and at the registration stage requires two types of documents (the Charter and the Corporation Establishment Agreement), which substantially increases the complexity and the length of registration process and hence decreases the attractiveness of this form of legal entity for investors. Even in Germany, which has been used as the model for the new Russian legislation, shareholders are not entitled to such appraisal rights[5]. The role of the courts in implementation of the provisions of corporate law is still weak due to the lack of professional experience and well qualified judges because of the low remuneration. The vast majority of companies maintain that they face major issues in protecting their interests in courts – the problem, which in our view is even more significant than lack of legislation.

6. Conclusions

To date, the state regulation of corporate sector is mostly focused on corporate governance standards for open companies that can give more regulatory power to state regulatory bodies, which to a large extent explains why the government intends to strengthen the corporate governance rules for public companies even further. At the same time, the largest part of corporate sector - the "closed" companies are beyond the radar screen of regulatory bodies and law-makers. The government agencies try to follow two different approaches at the same time - one toward a further market liberalization and wide implementation of principles of corporate governance, the other toward a further strengthening of the role of the state in the economic affairs. Yet, even in cases of open companies which must comply with ever increasing complexity

[5] In rare exceptions when these rights are granted, the doctrine of "corporate veil" is applied, which deprives them of protection of limited liability.

of government regulations in the area of corporate governance, civil servants in responsible government agencies are not exactly sure what represents good corporate governance practices. As a result, government representatives on corporate boards usually vote against having independent directors, retaining a corporate secretary, and detailed information disclosure to shareholders.

The current structure of the Russian corporate sector, the early development stage of the banking sector and the stock market, and the prevalent way the corporate sector is financed makes the Russian situation very different from that described by the Anglo-Saxon or the Continental Models. "Open" and "closed" companies in Russia have different economic drivers and market behavior, which makes corporate governance important (in a narrow definition sense) only for the former. However, if there is at least one thing that both types of companies have in common at this stage - it is the increasing government interference with their business.

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