The effectiveness of corporate governance policy in Greece

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Abstract

Purpose – The effectiveness of corporate governance enforcement is a complex issue requiring the understanding of the role of institutional factors. The latter may or may not converge towards best practices, depending upon the extent to which history and politics matter more than purely economic or efficiency-related considerations for convergence. The appropriateness and effectiveness of corporate governance enforcement mechanisms differ among market economies and cannot be attributed to one single factor nor does any such factor have the same significance in all countries as it depends on the relative state of development of financial intermediation. This paper aims to address these issues.

Design/methodology/approach – A critique is launched on the hypothesis of legal conformity used to explain the deviation of corporate governance practices and enforcement efficiency from is considered as best practice. The critique follows an historical development approach and is substantiated with some new empirical evidence of ownership structures and market views.

Findings – Empirical evidence on ownership structures and on the market views regarding the effectiveness of corporate governance legislation shows that for an understanding of the relationship between financial intermediation and corporate governance broader institutional influences must be taken into consideration.

Research limitations/implications – The analysis of empirical evidence needs detailed expansion and proper association with institutional elements to provide a more comprehensive understanding of corporate governance enforcement efficiency.

Practical implications – The exercise of corporate governance enforcement is an interactive process that goes beyond the role of legal rules and must combine an optimal set of private and public mechanisms properly tailored to each corporate governance regime.

Originality/value – New empirical evidence is provided on ownership structures and on the market view regarding the effectiveness of corporate governance legislation and a broader account is provided on institutional setting for understanding corporate governance policy.

Keywords Corporate governance, Ownership, Institutions, Greece

Paper type Research paper

1. Introduction

The publication of the *OECD Principle of Corporate Governance* (1999, 2003) and the *Principles of Corporate Governance in Greece* (1999) in the late 1990s led to fruitful debates on corporate governance in Greece, which however inclined at that time to view corporate transparency and accountability as rather "apocryphal" matters (Avlonitis and Mertzanis, 2002). Since then, the domestic implementation of a large number of EU directives, regulations and communications, the rise of diversified capital needs of Greek corporations within the new international environment of intensified financial competition and the gradual transformation of domestic corporate culture brought significant change in corporate relations and behavior. Corporate governance

JEL classification – K22, K42, G34

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problems have appeared during the past decade but were not associated with major scandals threatening the integrity of the Greek market. Most corporate governance problems and conflicts were depicted and dealt with by regulation and auditing. However, these changes and their market impact have not adequately been assessed. Public debate on corporate governance in Greece has been stalled.

In a recent paper in this journal, Lazaridis (2010) raises the issue of feasible and effective enforcement of corporate governance legislation in Greece. Drawing on relevant studies on corporate ownership and governance structures, Lazaridis argues that Greece is safely classified among the Continental European corporate governance pattern characterized by concentrated ownership, a dominant role for majority shareholders and a weak market for corporate control. He then argues that the provisions of the law 3016/2002, an important legislative initiative of corporate governance reform in Greece, are a mimic of SOX provisions in the USA aiming at encouraging capital inflows and that broadly speaking the former law has had no. effect on improving the fundamental elements of the Greek corporate environment. On account of divergent views as to the need for and efficiency of corporate governance reform, Lazaridis seems to favor legislative initiatives based on a conviction that the law should be simple, direct, easy to apply, holistic and fair as well as innovative in order to guarantee market order and fairness and ultimately safeguard market stability.

In assessing the current corporate governance regime in Greece, Lazaridis takes the view that the corporate governance framework is confined in the voluntary *Principles of Corporate Governance in Greece* (1999) and the law 3016/2002, which is deemed to be ineffective. On the basis of econometric tests, based on formal models implicitly in the tradition of law and finance analysis, he argues that performance modeling has not produced good fitness indicators that is standard organizational and decision-making factors are shown not to be statistically significant, which is interpreted as a factor distinguishing Greece from Anglo-Saxon countries. Thus:

> [. . .] while the relation of performance, CG and other factors of organizational, power and decision-making structure of firms have been well documented theoretically and empirically for the Anglo-Saxon countries or countries that have the same characteristics with them.

in Greece "[. . .] financial performance of firms seems to be unrelated to the previously mentioned factors" (p. 378).

These findings lead him to believe that product market competition and macroeconomic factors are the most probable factors explaining financial performance of listed companies in Greece.

Lazaridis argues that the relative underperformance of Greek firms is the result of inefficient enforcement. He postulates that:

> [. . .] all initiatives (Capital Market Commission Principles and Guidelines, Legal (law 3016/2002) and voluntary by the Hellenic Federation of Enterprises) could not convince stakeholders to change their attitude and perspective on their role, scope and range of activity and intervention. Minority shareholders remain, in reality, without any option, but the one of loyalty. Lack of capital market mechanisms and liquidity, as well as the unquestioned dominance of major shareholders, deprives minority shareholders from any other option (exit or voice) (p. 378).

Moreover, "[. . .] the other interesting point is that executive remuneration is not dependent on performance, power and control structure, monitor efficiency and incentive plans". Such inefficiency is moreover a domestic feature, since:

> […] the law (i.e. 3016/2002) failed to establish an independent monitoring mechanism or to enhance the efficiency of the existing ones, i.e. internal control, unlike SOX Act's 404 section that promotes the constant improvement of internal control system. By doing that, the law did not change the capital structure preferences and did not challenge the current status quo within the firm.

Further, according to Lazaridis, the inefficient enforcement is due to the inadequate enforcement by the securities regulator:

> […] the […] HCMC has failed to enforce rules and regulations. HCMC's annual reports indicate that although a number of violations have been spotted and documented, No. penalties or other administrative actions have been imposed. HCMC uses the inefficient judicial way of enforcement.

And, finally:

> […] the main cause of legal ineffectiveness and disarray between corporate environment and legal provisions is that the legislators did not take into account the fundamental elements the Greek corporations.

Lazaridis' assessment of corporate governance legislation is a welcome step in understanding the impact of regulatory reform in Greece. He provides some useful evidence of the impact of regulatory reform. However, this paper argues that Lazaridis' view on the underperformance of Greek firms and on the causes for underperformance resting mainly on the inefficiency of legal enforcement is overall ill-conceived and not warranted by the facts. First, Lazaridis' analysis does not take into consideration that corporate governance reform within a broader regime includes numerous legislative initiatives in the areas of shareholder rights, transparency and disclosure of financial and non-financial corporate information, takeover bids and company law, which implement a wide range of EU directives, regulations and communications. The initial provisions of the law 3016/2002 were subsequently improved by supplementary provisions in several other legal acts, including a 2007 amendment of company law 2190/1920. Second, and more importantly, his interpretation of results based on an amalgamation of formal models lead him to conclusions that are too strong, as his formal analysis does not take properly into consideration the institutional nature of corporate governance arrangements and enforcement efficiency as well as the complex interactions between financial intermediation, law enforcement and corporate governance. These interactions must be understood if efficient policy making is sought for.

This paper is concerned with the second issue only. It argues that any divergence of national corporate governance practices from those recognized as best ones implies a question of why different corporate governance systems have not converged towards the economically best system at a rapid pace, which in turn raises the issue of the extent to which history and politics matter more than purely economic or efficiency-related considerations for convergence. Moreover, while the extent of effective enforcement of contractual agreements is a most important determinant of economic performance of firms, the inappropriateness and ineffectiveness of corporate governance enforcement mechanisms differ among market economies and cannot be attributed to one single factor (i.e. inefficient regulator) nor that any such factor has the same significance in all countries as it depends on the relative state of development of its financial system. It is argued that the efficiency of corporate governance enforcement can be better understood once a proper and adequate account is made of ownership and governance structure development, highlighting the fundamental impact of institutional factors. To substantiate the arguments, the paper provides some new prima facie empirical evidence on ownership structure and market view on corporate governance reform.

In the remainder of the paper, Section 2 analyzes the role of institutions for financial development. Section 3 analyzes the relationship between patterns of corporate governance in different financial systems as well as the transformation aspects of corporate governance along with different patterns of financial intermediation. Section 4 comments on the relationship between corporate governance frameworks and economic growth. Section 5 refers to the specific circumstances shaping corporate governance in Greece, and finally Section 6 comments on efficient corporate governance policy.

2. Institutions, path dependence and financial development

There is widespread agreement that institutions shape economic outcomes and are important determinants of financial market development. However, the channels through which institutions provide incentives for investment and influence corporate behavior are not yet fully understood. Institutions involve both formal constraints based on self-devised and imposed human rules and informal constraints such as conventions and rules of behavior (North, 1990). Understanding the role of informal institutional constraints is a crucial component of predicting the impact of formal institutional change and of making appropriate policy recommendations. It is relatively straightforward to change formal institutions by altering the legal rules that govern society, but it is much more challenging to change informal institutional constraints that manifest themselves in culture and norms of behavior.

Corporate ownership and governance structures depend on corporate conventions and rules of behavior; hence, evolution and convergence of corporate structures depend to a large extent on the evolution and convergence of corporate conventions and rules of behavior. For structural convergence to occur, corporate conventions and rules of behavior must converge. However, because of powerful path dependent and other institutional reasons corporate conventions and rules of behavior among different economies might not converge (Bebchuk and Roe, 1999; Schmidt and Spindler, 2002). Even if state bureaucracies were efficient, a country's corporate conventions and rules of behavior might be path dependent, as they depend both on the country's initial corporate governance structures, including tradition, interest group politics and foreign influence. The initial pattern of a country's corporate structures has created interest groups and accordingly determined their power to influence the pattern of evolution of corporate rules. If a pattern of ownership and governance creates a group with positional advantage inside the firm and society, that group will often have the motivation and the means to preserve rules that favor itself.

Given that factors determining efficient institutional arrangements change over time, a once efficient arrangement or enforcement mechanism may become inefficient from today's perspective. That is, given that the possible efficiency or welfare gain brought about by changing an institutional arrangement may not be sufficient to cover the costs of adjustment, society might rationally keep the seemingly inefficient institutions.

Consequently, the rules and conventions that a country will have down the road will depend on the type of corporate structures and corporate rules that it began with.

Once a country has rules and conventions that favor, for example, powerful professional managers over shareholders or other corporate constituencies, these managers will want to fight off a change in rules and often they will have the resources to do so. Similarly, a country whose rules favor, for example, concentrated shareholders over minority shareholders will have a powerful interest group, namely the concentrated owners, who will want to fight off a change in rules. And similarly, a country whose rules favor stakeholder participation will not easily reverse course.

Moreover, depending on the initial conditions, the efficiency of local governance structures is often path dependent: sunk adaptive costs and network externalities may impede necessary structural change. Furthermore, even inefficient governance structures may tend to persist, owing to an insufficiently high level of transactions activity that could act as a catalyst for structural transformation. Thus, if higher transactions activity in a firm results in a reduction of the company's controlling shareholder's wealth, then the controlling shareholder might impede the company from further diffusing ownership, even if diffusion would be overall efficient for the company. And management might impede their company from moving to concentrated ownership even if moving there would be overall efficient.

Thus, the question is whether the powerful forces of modern rapidly globalizing product and capital markets do succeed in inducing adequate structural change and convergence in any given corporate governance regime. At the macro level, globalization, competition and rules reform put pressure on companies to change and adopt more efficient governance practices. But, equally, companies face powerful pressure to stay on their given path, so the resultant speed and direction of corporate governance transformation would then be an empirical question and, given the strength of the forces of persistence, it is doubted whether the result will be complete and rapid convergence will emerge, allowing for a wide variety of different structures to persist.

There is a substantial body of evidence on the role of institutions for financial development based on cross-country studies which reveal both formal and informal aspects of institutional impact. A growing number of studies show that the ability of a country's institutions, conventions and rules of behavior to protect shareholder rights and provide incentives for investment is a key explanation for the persistent disparity in and efficiency of financial market development (see from different persuasions, Knack and Keefer, 1995; La Porta *et al.*, 1997, 1998, 2000; Levine, 1997, 2002; Levine *et al.*, 2000; Rajan and Zingales, 2001, 2003; Beck *et al.*, 2000, 2003; Acemoglu *et al.*, 2001; Armour *et al.*, 2008, 2010).

The institutional nature of corporate governance arrangements means that testing for the hypothesis of legal conformity, as Lazaridis does, implies that comparisons must at least be made not only on the basis of laws on the books (law extensiveness) but also on differences in enforcement (law effectiveness) which take into consideration other economic and institutional factors (Pistor *et al.*, 2000, 2003). For example, empirical evidence on insider trading shows that it is not the presence of laws but rather actions against insider trading that help explain the development of securities markets (Bhattacharya and Daouk, 2002).

3. Financial intermediation and corporate governance

Corporate governance efficiency depends on the financial intermediation structures. On the one hand, financial intermediation has historically endeavored to bridging the information gap between borrowers and lenders of funds; lenders do not know if borrowers intend to repay interest and principal (Akerlof, 1970). Intermediation also minimizes agency problems by mitigating potential conflicts of interests among managers, shareholders and debt holders (Jensen and Meckling, 1976). Solutions are found in corporate law, capital market law, takeover law and capital market discipline. On the other hand, corporate ownership and governance structures depend on differing cultural, social and political factors and legal origins (civil vs common law) across economies (Black *et al.*, 2010; Barca and Becht, 2000, 2001). Anglo-American common law governance structures are characterized by ownership dispersion and emphasize the maximization of shareholder value subject to various versions of bankruptcy law and strong market discipline, to be exercised through the market for corporate control, to ensure that managers are committed to the pursuit of shareholder value and the maximization of returns for shareholders. Continental European and Asian civil law governance structures are characterized by ownership concentration and emphasize the disciplinary role of banks and controlling interests in rather illiquid equity markets characterized by interlocked companies subject to minority shareholder rights protection and insider dealing rules.

Alternative modes of financial intermediation and corporate governance have been identified (Levine, 1997, 2002; Tadesse, 2002) competing or complementing each other: the bank-based view, the market-based view, the financial services view, the law and finance view and the political economy view. Those working within these areas promote the merits of their own view. Each of these views is briefly discussed in turn.

First, advocates of the bank-based view argue that in less-developed countries banks are more effective than markets in financing industrial expansion (Gerschenkron, 1962; Boot and Thakor, 1997; Boyd and Smith, 1998; Allen and Gale, 2001). Owing mainly to inadequate development of bond and equity markets as well as inadequate regulatory control over financing activities, commercial banks take the lead in financing industry restructuring and investment and by virtue of commanding better information exercise a strong monitoring role on prudent behavior. In weak market systems, concentrated bank ownership, poor accountability structures, weak property rights for investors and a non-independent judiciary may be observed, collectively allowing for more frequent market abusive practices (Batten and Kim, 2000). In such circumstances, legal and regulatory reform is likely to be as important as financial market reform.

Second, advocates of the market-based view argue that dominant and influential banks in controlling the financial system hamper competition and therefore the growth of smaller institutions. Banking-sector reform takes time and structural problems in the banking sector cannot easily be overcome. These activities would be detrimental to domestic financial development and restrain successful corporate control (Hellwig, 1998; Wenger and Kaserer, 1998). Moreover, strong state-owned banks will lead rather to inefficient resource allocation since they are more likely to focus on political goals, such as channeling credit to labor-intensive industries (La Porta *et al.*, 2002). Therefore, market-based finance is necessary to ameliorate the negative consequences of powerful banks and encourage innovation. Thus, regulatory reform must aid market competition, thereby enabling risks to be diversified, increasing market liquidity and encouraging the production and dissemination of lower cost information as a conditions for efficient decision making in the areas of financing and innovation (Allen and Gale, 2001; Levine, 2002). The role of investor protection measures and of credit rating agencies in assessing the credit quality of investments becomes important. However, markets are costly to use, expose investors to market risk and destroy risk-sharing opportunities.

Third, advocates of the law-and-finance view argue that the existence of a properly functioning legal system is crucial for the development of a financial system. Unlike other enterprises, financial institutions can only be established by proper authorization and operate under rules from regulatory agencies, making the legal system a necessary component of any financial system (Benston and Smith, 1976; La Porta *et al.*, 1998, 1999). It is only when proper regulation and legal frameworks are in place that the financial system is truly competent and can function efficiently and effectively. It is only when the investors are legally protected, making all contracts binding, that external financing and capital allocation efficiency are achieved. This view of the financial system encompasses both bank- and market-based perspectives. What distinguishes undeveloped from developed financial markets is the absence of the supporting legal framework to protect investors and other stakeholders from abusive transactions.

Fourth, advocates of the financial services view stress the importance of the diversity of financial services for improving information and transaction costs (Levine, 1997). Banks and markets might act as complements in providing such services (Boyd and Smith, 1998; Huybens and Smith, 1999). Although the law-and-finance view states that contractually enforced transaction mechanisms and the legal framework are pivotal to fostering economic growth, a financial system, by efficiently providing developed and diversified financial services, aids liquidity, risk management and the exertion of corporate control, thus fostering economic growth (Levine, 2002). The impact is higher if a functional rather than an institutional perspective is applied (Allen and Santomero, 2001) and if an improvement in enforcement mechanisms precedes financial system stability and development (Bryant, 1988).

Fifth, advocates of the political economy view stress that ownership structures and financial development is the outcome of socio-political processes and decisions. This view is dynamic in nature, since changes in the political power of different constituencies can alter a country's disposition towards financial development. As with any political decision, financial development is the outcome of ideology and the economic interests of voters and pressure groups. Thus, stock market development may be fostered or hampered by government action depending on the balance of power among interest pressure groups (Rajan and Zingales, 2003), state intervention in the economy may conflict with financial development because the state acts as a substitute for financial markets (Pagano and Volpin, 2000; Biais and Perotti, 2002), and financial market development may be retarded due to the lobbying by incumbent families to prevent entry of potential competitors aiming at preserving their own vested power (Perotti and von Thadden, 2003; Perotti and Volpin, 2004). One prediction of these political economy theories is that financial development should be negatively related to state ownership. Another is that ownership should be more concentrated and companies should be organized into groups in countries where the government has a big role in the economy (Pagano and Volpin, 2006). When the state has a great involvement in the economy, firms need political support to grow. Hence, to maximize their political clout, entrepreneurs need to maximize the value of assets under their control. With concentrated ownership and pyramidal groups, both goals are attained. If the government has a more limited involvement in the economy, political connections are less important. Hence, pyramidal groups and concentrated ownership are less diffuse.

Which one of the aforementioned modes of financial intermediation and corporate governance best describe the development of the Greek market? The critical issue here is ownership structure. Very few relevant studies exist for Greece and these focus on the more narrow relationship between some measure of corporate ownership and performance. In these studies, ownership is approximated by either the fraction of shares owned by management and significant shareholders over 5 percent in 175 firms for the year 2000 (Kapopoulos and Lazaretou, 2007), or by insiders' stakes in 59 firms for the period 1996-1998 (Karathanassis and Drakos, 2004), or by ownership concentration indices in 60 firms for the period 2001-2006 (Lazaridis *et al.*, 2009). The evidence presented in those authors presents only a limited view of the development of ownership structures underlying the dominant mode(s) of financial intermediation and corporate governance in Greece. A contribution on revealing the modern ownership structure of listed corporations in Greece is made below.

Table I presents some new prima facie evidence on ownership structure in Greek listed firms on the basis of ownership stakes over 1 percent from all 270 firms in the Athens Exchanges for the year 2009. Reported values represent direct owners holdings for each listed company in both absolute terms and weighted by the company's relative capitalization level to take account of company size. The analysis shows that in the total sample, the mean absolute value of all owners is the rather low 10.7 percent and the median is the lower 3.4 percent. The respective mean and median cap-weighted values are 0.037 and 0.002 percent. At first sight, financial companies (banks, investment companies and insurance companies together) do not seem to play a decisive role in influencing corporations through direct ownership claims (the mean absolute value of financial companies as owners is 12.2 percent and the median is 3.2 percent, whilst the respective mean and median cap-weighted values are 0.035 and 0.002 percent). Financial companies are shown to own a rather small relative stake of 6.594 percent in total ownership. On the other hand, the importance of the state is evident. The state is one of the largest shareholders and that is more so in the biggest listed companies (the mean absolute value of the state as an owner is 29.8 percent and the median is 21.9 percent, whilst the respective mean and median cap-weighted values are 0.520 and 0.186 percent). Thus, the state is shown to be in a firm position to exercise effective control on large companies. Minority shareholders, who are taken to mean all shareholders that collectively own less than 1 percent of a listed company's shares, seem to play an important role too, since the mean absolute value of them as owners is 26.4 percent and the median is 23.2 percent, whilst the respective mean and median cap-weighted values are 0.156 and 0.006 percent, thus indicating a substantial dispersion of ownership. Minority shareholders are shown to own a rather large relative stake of 44.39 percent in total ownership. Foreign investors as a whole are also prominent shareholders in Greece but they own small stakes (the mean absolute value of foreign investors ownership stake is 6.6 percent and the median is 2.5 percent, whilst the respective mean and median cap-weighted values are 0.040 and 0.004 percent). As a whole, foreign investors own a rather large relative stake of 24.66 percent in total ownership. Finally, the very high maximum values reported for ownership holdings represent those few companies which have taken a squeeze-out approach in order to be de-listed.

Owner type	Stat.	Share ownership (%)[a]	Cap-weighted share ownership (%)[b]
Minority shareholders[c]	Mean	26.4	0.156
	Median	23.2	0.006
	Min.	1.0	−0.009
	Max.	95.1	11.374
	Sum	–	44.392
Natural person	Mean	8.9	0.007
	Median	3.0	0.001
	Min.	1.0	0.000
	Max.	97.0	1.914
	Sum	–	9.435
Institutional investor	Mean	2.7	0.016
	Median	1.6	0.002
	Min.	1.0	0.000
	Max.	42.4	0.445
	Sum	–	2.190
Pension fund	Mean	1.4	0.035
	Median	1.4	0.035
	Min.	1.3	0.001
	Max.	1.4	0.070
	Sum	–	0.071
Financial company	Mean	12.2	0.035
	Median	3.2	0.002
	Min.	1.0	0.000
	Max.	96.7	2.037
	Sum	–	6.594
Manufacturing/agricultural Co.	Mean	18.8	0.032
	Median	5.1	0.004
	Min.	1.0	0.000
	Max.	88.7	0.392
	Sum	–	2.050
Commercial/services Co.	Mean	12.9	0.016
	Median	4.4	0.002
	Min.	1.0	0.000
	Max.	95.4	0.286
	Sum	–	1.327
Foreign investor	Mean	6.6	0.040
	Median	2.5	0.004
	Min.	1.0	0.000
	Max.	97.1	2.220
	Sum	–	24.066
The state	Mean	29.8	0.520
	Median	21.9	0.186
	Min.	1.8	0.000
	Max.	75.2	1.993
	Sum	–	9.888
Total	Mean	10.7	0.037
	Median	3.4	0.002
	Min.	1.0	−0.009
	Max.	97.1	11.374
	Sum	–	100.000

Notes: [a]Percent value of the different owners holdings for each listed company; [b]percent value of the different owners holdings for each listed company i, weighted by the company's relative capitalization level ($w_i = Cap_i/Cap_{market\ total}$, $i = 1$ to n, and $n = 270$ firms listed in the Athens Exchanges); all individual owners' cap-weighted share ownership percentages add up to 100 percent for the entire market; [c]minority shareholders are taken to mean all shareholders that collectively own less than 1 percent of a listed company's shares

Source: Data on ownership structure include direct shareholdings over 1 percent in all companies listed in the Athens Exchanges as maintained by the securities dematerialization system in Greece

Table I.
Ownership structure in Greece, 2009

This prima facie evidence shows that ownership structure in Greek listed companies has been subject to substantial change since earlier accounts and certainly casts doubt on any painless classification of Greek ownership structure in the Continental European ownership pattern characterized by concentrated ownership and a dominant role for majority shareholders, including a strong monitoring role of banks. Further analysis is needed to provide a fuller picture of the development and modern shape of ownership structures and their relationship with financial intermediation and corporate governance patterns in Greece. Next, we turn into the subsequent relationship between corporate governance and the economic performance.

4. Corporate governance and economic performance

Recent finance literature shows a positive link between the level of financial sector development, financial performance of firms and economic growth (Allen and Gale, 2001; Levine, 2002). This link also suggests a significant role for corporate governance and property rights in securing these positive economic outcomes. The theoretical foundations for these arguments are provided by the law-and-finance view culminated in La Porta *et al.* (1998, 1999, 2004, 2006, 2008) (hereafter referred to as LLSV) and their followers. The central proposition of the LLSV view is that there is a systematic causal relationship between the legal framework, the corporate financing patterns, corporate behavior and performance and overall economic growth. The LLSV analysis is based on an empirical and theoretical evaluation of different legal systems (i.e. common and civil law traditions) whose historical origins are exogenously determined. This view underlies Lazaridis' analysis too.

According to the "legal origin" hypothesis, legal differences between countries can be categorized, quantified and analyzed. Common law countries are associated with higher protection for shareholders and greater rights for creditors than do civil law countries. The legal systems not only differ with respect to protection for shareholders, but also with respect to labor, contract enforcement and self-dealing rules, among other attributes. Legal enforcement efficiency differs too. Common law works better than civil law and is more conducive to economic development because in common law countries judges interpret the law whereas in civil law countries judges are bound by long explicit laws and codes, leaving them with little discretion. Anglo-Saxon model based on English common law are considered most conducive to the protection of shareholders, by safeguarding property rights and the enforcement of contracts. As a consequence, common law country firms have greater access to outside finance, are less subject to government control and have faster corporate growth, which in turn cause faster growth of national income.

However, the positive link between the legal origin hypothesis, financial sector development and economic growth is not based on systematic theoretical analysis or rigorous empirical research. There are several significant lines of criticism against at the underlying LLSV view of legal origin in substantiating the link between legal systems, financial development and economic performance.

First, the theoretical framework presented in LLSV is far too limited for examining corporate governance issues in developing countries (Berglöf and von Thadden, 1999). LLSV appear to be solely interested in the question of the protection for providers of external finance to the exclusion of other significant stakeholders in the firm. Whilst the reference point for the LLSV study is the widely held, Berle and Means-type corporation which is prevalent mainly in the USA and the UK, the typical firm in developing countries is rather a family controlled or closely held by block holders, i.e. it has concentrated share ownership. The important corporate governance problem for this class of firms is not legal protection for outside shareholders but rather the problems of family succession and maintaining family control while raising funds from outside investors.

Second, the econometric basis for the LLSV argument is also susceptible to important methodological limitations. As Arestis and Demetriades (1997, 1999) noted, most of the studies are based on reduced form analysis and are therefore difficult to interpret in causal terms. They also ignore altogether the evidence presented in the earlier sections on the observed inefficiencies of the pricing and takeover mechanism on the stock markets. Thus, the direction of causality between legal system and financial structure could run in either direction. The legal system may lead to the formation of a certain financial structure, as LLSV maintain, but it is at least equally plausible that the financial structure may also lead to the creation of legal norms. It is important to note that even on its own terms, maximizing legal investor protection cannot be optimal. It will result in the dilution of efficiency advantages deriving from the lower agency costs of concentrated ownership.

Third, over the past 50 years there have been major changes in the economic regime and in the role of stock markets in many countries, which have occurred without any fundamental changes in those countries' constitution, basic legal framework or its legal origins (Glen *et al.*, 2001). Rather, the law has shown itself to be able to accommodate the needs and desires of economic policy makers, involved with achieving political independence and equitable patterns of development as well as devising industrial and privatization strategies. The law did not deter, nor became a prime mover, but only a handmaid to politics and reform.

Fourth, the "legal origin" hypothesis is recently disputed by the modern scholars of corporate law and finance in accordance with the results of an interdisciplinary research project on law, finance and development based on new longitudinal data on legal protection of shareholders', creditors' and labor rights (Armour *et al.*, 2008, 2009, 2010; Fagernäs *et al.*, 2008; Sarkar and Singh, 2009). These authors argue that what has emerged from the interaction of theory and evidence over the past decade is not so much legal rules themselves that matter, as is the infrastructure of the legal system. Legal infrastructure refers to the meta-level rules, norms and practices which determine, in a given national context, the mechanisms for lawmaking and dispute resolution, the competencies of legislatures and courts and the conception of the role of government in the economy and society, among other things. In this broad sense, "legal origin" should not be confined to formal legal institutions (as the LLSV argue for), but may extend to include informal norms and shared assumptions about the prevailing style of social control of economic life which is endogenously determined by a country's structural transformation path. On this basis, these scholars argue that, first, the narrow technical finding that the "legal" origin hypothesis concerning shareholder protection and stock market development is not sustained by the analysis of the longitudinal data for various institutional reasons, such as the manner in which judges interpret the law, and, second, that the use of the "legal origin" hypothesis as a basis for suggesting legal reform according to common law standards to foster economic development is ineffective. Instead, it should be recognized that each country has its own form of capitalism and its own legal and regulatory institutions, and that there is no. single development and enforcement model which can cover all their needs. The unqualified implementation of the LLSV approach to the interpretation of the emergence and efficiency of national financial and governance structures essentially shows not the latter's overall efficiency but rather their relative deviation from the Anglo-Saxon structures.

In addition to the aforementioned specific LLSV criticisms, further more general criticisms on the relation between financial sector development and economic growth are advanced. First, the produced evidence is rather inconclusive, even though available research seems to highlight a profitability-enhancing role of dominant owners (Short, 1994; Gugler, 2001). The studies surveyed analyze mostly the US and the UK experience and use as dependent variables proxies for corporate performance (net income to net worth ratio, rate of return on equity, Tobin's Q, and total factor productivity) or for the riskiness of returns (variance and skewness of profitability). The studies make use of a rather arbitrary classification between manager-controlled and owner-control firms, on the basis of a specific percentage ownership criterion (say over 5 percent) for a single block of voting stock or other concentration measures. No. explicit differentiation is made between ownership and voting rights, implicitly assuming that the "one-share-one-vote" principle prevails. More recent studies focused less on the distinction between manager-controlled and owner-control firms and more on ownership concentration and managerial and board ownership.

Second, the adoption of an institutional approach to understanding corporate governance arrangements and their enforcement efficiency has to deal with the issue of proper measurement of institutional quality (Glaeser *et al.*, 2004). Much of the empirical work in corporate governance purports to shed light on the relative weight of counteracting institutional mechanisms. It usually involves a regression of some measure of corporate performance on measures of the stringency of corporate governance, such as ownership structure, capital structure, the structure of the board and the market for corporate control. However, empirical studies on corporate governance have more than the usual share of econometric problems (Börsch-Supan and Köke, 2000). Quite frequently, firm variables are assumed to be exogenous but are actually endogenous affecting the direction of structural causality and allowing for spurious correlation, relevant variables are left out, the sample is not selected randomly, and variables are measured with large errors. In all of these cases, it will be difficult to identify the influence of corporate governance factors on firm performance.

Thus, notwithstanding the weak theoretical and empirical foundations of the legal conformity hypothesis as a basis for understanding the relative effectiveness of corporate governance enforcement regime in Greece, Lazaridis's (2010, p. 378) claim, that the low goodness of fit of his econometric results should be interpreted as that financial performance of Greek firms is unrelated to standard corporate governance characteristics, should have been made with the most caution on econometric grounds alone. More detailed specification of the models and proper consideration of special methodological and interpretational issues such as arbitrariness of classification, choice of endogenous variables, the extent of omitted variables, sectoral effects, reverse causality, or simultaneity between control devices, are necessary before more definite results obtain and conclusions made.

In general, the empirical studies on the positive link between the level of financial sector development and economic growth lead to the conclusion that a financial system, irrespective of whether it is bank based or market based, can serve as a catalyst to economic growth by providing sound financial services in a regulated environment. The outstanding success over the past 40 years of both Japan and Germany, with their bank-based systems, and of the alternative market-based systems evident in the USA and the UK is testament to the success of each of these approaches in securing financial development, sound corporate performance and strong economic growth. However, the understanding of the precise channels through which this has been possible, rests on a lot more than a mere analysis of the role of legal systems and requires a broader institutional approach to understanding the development of financial intermediation and corporate governance patterns in each country, in accordance with the "varieties of capitalism" approach, which begins from the premise that economic and business systems are organized in different ways in different countries.

5. The efficiency of corporate governance enforcement

Corporate governance practices essentially aim to enhance investor commitment and ensure that management is devoted to choosing efficient projects, disclosing relevant information and ultimately providing an accepted return to investors, thus lowering their risk of fraud or deception. Depending on the extend of internal and external pressure and path-dependent influences, corporate governance practices are affected by different institutional arrangements and may coexist side by side even though they differ with respect to the efficiency with which they fulfill the same function.

Different enforcement mechanisms can be deployed to ensure commitment and overcome investors' concerns, depending on a country's institutional development and contracting environment. Some potentially important mechanisms may be hard to influence through policy choices, whilst other potentially less important ones may be susceptible to policy intervention.

Corporate governance enforcement systems can be both private and public (Berglöf and Claessens, 2004). Private initiatives to enforce contracts can operate outside the legal system and may take the form of individual firm initiatives (e.g. reputation building) or of a coordination and cooperation among firms (e.g. mutual integration, industry associations with private conflict resolution and enforcement). Private arrangements can later be standardized and encoded in public law, which may be enforced privately through litigation, or publicly by the state. Under private law enforcement, private agents act within a legal or regulatory framework to punish contractual violations, using the courts to adjudicate and the state to enforce the final judgment. Under public enforcement, the government provides the final enforcement system and acts as prosecutor.

An enforcement system may consist of a number of interactive private and public enforcement mechanisms of different severity, mutual complementarity, state intervention, regulatory capture and tradeoff between costs and benefits (Djankov *et al.*, 2003). The effectiveness of private enforcement mechanisms depends on the effectiveness of public enforcement mechanisms, as the latter reduce the costs of the former.

The efficient choice of enforcement mechanisms depends largely on the overall institutional environment. For example, in an institutional environment characterized by efficient cooperation among public and private agents as well as high levels of information, resources, and incentives for private agents, enabling them to exercise strong market discipline, public enforcement through direct state intervention is less important. Moreover, in an institutional environment characterized by the existence of powerful controlling owners and/or managers, public enforcement through direct state intervention is less effective, as those owners and managers will most eventually find a way to circumvent the system. Further, in an institutional environment characterized by strong and efficient public enforcement institutions, private enforcement of public law through litigation and court intervention is more efficient.

In order to highlight some aspects of the relevant importance of private-public enforcement mechanisms in Greece, we present some of the results of a market inquiry carried out in 2010 by the securities regulator in Greece (HCMC) in association with the Federation of Greek Industries on the efficiency and effectiveness of prevailing corporate governance arrangements and in particular of the law 3016/2002. Table II presents some of the responses offered by the companies listed in the Athens Exchange to questions asked in a questionnaire sent to them.

This prima facie evidence shows that, on the general issue of corporate governance efficiency, 72.4 percent of the respondents judged the quality of corporate governance practices prevailing in Greece to be of an average level (with a substantial dispersion of views: SD = 53.17 percent) and a high 84.2 percent of the respondents have the view that the quality of corporate governance practices would improve as a result of applying both external rules and internal codes of ethics (with substantial dispersion of views: SD = 52.56 percent). The fact that the overwhelming majority of the respondents have the view that corporate governance practices would improve by both means, while only 10.36 and 5.41 percent of them accepting, respectively, private only and public only enforcement as an adequate mechanism of overall corporate governance improvement, indicates that the respondents seem to share the common view that efficient enforcement of corporate governance is the result of cooperation between the private and the public sector. Interestingly, such a view may reflect a market's weak belief in the efficiency of both the role of government/regulator and of market discipline alone in bringing about efficient corporate governance outcomes. Moreover, it may not coincide with what the prevailing ownership patterns (Table I) would like us to expect.

On the special issue of the effectiveness of law 3016/2002, the disclosed market view is equally interesting. Indeed, an overwhelming 93.67 percent of the respondents have the view that the law 3016/2002 has had a positive impact on improving the composition of the board of directors, 88.24 percent view a positive impact on improving the function of the board, and 61,64 percent view a positive impact on improving the decision making of the board, but only 52.05 percent of the respondents have the view that the law has had a positive impact on improving the overall efficiency of the board. Similar conclusions may be drawn from the examination of the responses on the issues of board transparency and director independence and remuneration. Thus, regardless the perceived positive impact of external government regulation on improving the composition, function, transparency and decision making of the board, the market thinks that the overall efficiency of the board is not commensurably improved. This implies that the overall efficiency of the board is viewed by the companies to be only partially related to the improvement in the board's composition, function, transparency and decision-making process, which in turn implies that additional enforcement mechanisms would be necessary to achieve the task. Similar conclusions are broadly drawn from the other responses.

Table II. Market view on the impact of law 3016/2002 on corporate governance practices

Questions/statistics	Responses (numbers in percent) 1	2	3	4	5
How do you judge the quality of CG in Greece today? Stats: mean = 3, median = 3, and SD = 53.17 percent	Bad 9.50	Average 72.40	Very good 17.65	Excellent 0.45	
The quality of CG would improve as a result of applying: stats: mean = 3, median = 3, and SD = 52.56 percent	External rules only 5.41	Internal code of ethics 10.36	Both 84.23	–	–
1. Overall impact of law on improving the composition of the BoD: stats: mean = 1, median = 1, and SD = 44.81 percent	Positive 93.67	Negative 1.36	No. impact 4.98	–	–
2. Extent of impact of law in improving the composition of the BoD: stats: mean = 4, median = 4, SD = 95.66 percent	Very low 1.99	Low 9.45	Average 21.89	High 46.27	Very high 20.40
3. Overall impact of law on improving the function of the BoD: stats: mean = 1, median = 1, and SD = 61.84 percent	Positive 88.24	Negative 1.36	No. impact 10.41	–	–
4. Extent of impact of law on improving the function of the BoD: stats: mean = 3, median = 3, and SD = 85.62 percent	Very low 2.13	Low 10.11	Average 41.49	High 38.30	Very high 7.98
5. Overall impact of law on improving the efficiency of the BoD: stats: mean = 2, median = 1, and SD = 99.64 percent	Positive 52.05	Negative 0.91	No. impact 47.03	–	–
6. Extent of impact of law on improving the efficiency of the BoD: stats: mean = 3, median = 3, and SD = 100.86 percent	Very low 4.39	Low 20.18	Average 34.21	High 32.46	Very high 8.77
7. Overall impact of law on improving decision making of the BoD: stats: mean = 2, median = 1, and SD = 96.07 percent	Positive 61.64	Negative 1.83	No. impact 36.53	–	–
8. Extent of impact of law on improving decision-making of the BoD: stats: mean = 3, median = 3, and SD = 103.11 percent	Very low 7.35	Low 20.59	Average 38.24	High 26.47	Very high 7.35
9. Overall impact of law on improving transparency in decision making of the BoD: stats: mean = 1, median = 1, and SD = 80.29 percent	Positive 79.09	Negative 0.91	No. impact 20.00	–	–
10. Extent of impact of law on improving transparency in decision making of the BoD: stats: mean = 3, median = 3, and SD = 101.53 percent	Very low 4.73	Low 10.06	Average 38.46	High 31.95	Very high 14.79
11. Overall impact of law on improving the independence of directors' decision making: stats: mean = 1, median = 1, and SD = 84.49 percent	Positive 76.02	Negative 0.90	No. impact 23.08	–	–
12. Extent of impact of law on improving the independence of directors' decision making: stats: mean = 3, median = 3, and SD = 101.53 percent	Very low 1.85	Low 17.28	Average 27.16	High 37.65	Very high 16.05
13. Overall impact of law on improving training and education of directors: stats: mean = 2, median = 1, and SD = 99.53 percent	Positive 52.97	Negative 0.91	No. impact 46.12	–	–

(*continued*)

Questions/statistics	Responses (numbers in percent) 1	2	3	4	5
14. Extent of impact of law on improving training and education of directors: stats: mean = 3, median = 3, and SD = 112.82 percent	Very low 5.22	Low 20.00	Average 33.91	High 23.48	Very high 17.39
15. Overall impact of law on improving transparency of directors' remuneration: stats:: mean = 1, median = 1, and SD = 79.67 percent	Positive 79.09	Negative 1.36	No. impact 19.55	–	–
16. Extent of impact of law on improving transparency of directors' remuneration: stats: mean = 4, median = 4, and SD = 106.27 percent	Very low 4.68	Low 9.94	Average 20.47	High 43.86	Very high 21.05
17. Overall impact of law on improving the establishment of BoD committees: stats: mean = 1, median = 1, and SD = 86.14 percent	Positive 74.66	Negative 0.90	No. impact 24.43	–	–
18. Extent of impact of law on improving the establishment of BoD committees: stats: mean = 3, median = 3, and SD = 111.44 percent	Very low 6.75	Low 22.70	Average 28.83	High 30.06	Very high 11.66
19. Overall impact of law on improving the effectiveness of internal audit: stats: mean = 1, median = 1, and SD = 61.76 percent	Positive 88.64	Negative 0.91	No. impact 10.45	–	–
20. Extent of impact of law on improving the effectiveness of internal audit: stats: mean = 3, median = 3, and SD = 96.42 percent	Very low 2.60	Low 12.50	Average 35.42	High 35.94	Very high 13.54
21. Overall impact of law on improving the risk management functions of the BoD: stats: mean = 2, median = 1, and SD = 99.11 percent	Positive 55.25	Negative 0.91	No. impact 43.84	–	–
22. Extent of impact of law on improving the risk management functions of the BoD: stats: mean = 3, median = 3, and SD = 112.04 percent	Very low 9.02	Low 18.85	Average 32.79	High 28.69	Very high 10.66
23. Overall impact of law on balancing majority and minority interests in the company: stats: mean = 2, median = 1, and SD = 93.98 percent	Positive 66.82	Negative 0.46	No. impact 32.72	–	–
24. Extent of impact of law on balancing majority and minority interests in the company: stats: mean = 3, median = 3, and SD = 113.05 percent	Very low 8.97	Low 12.41	Average 40.00	High 23.45	Very high 15.17
25. Overall impact of law on improving communication of the company with its shareholders: stats: mean = 2, median = 1, and SD = 90.88 percent	Positive 70.59	Negative 0.45	No. impact 28.96	–	–
26. Extent of impact on improving communication of the company with its shareholders: stats: mean = 4, median = 4, and SD = 94.86 percent	Very low 1.32	Low 9.27	Average 33.77	High 35.76	Very high 19.87

Source: Data from the HCMC Questionnaire filled by the companies listed in the Athens Exchanges, July 2010

Table II.

It is evident that certain "irregularities" characterize the respondents' view regarding the factors affecting the efficiency of corporate governance enforcement, implying a need to look into factors that go beyond those perceived by standard corporate governance analysis and are properly located within the local institutional environment. Perhaps, political institutions, as part of the general enforcement environment may be perceived as poorly functioning or being captured by special interests. The level of enforcement may indeed interact with applied legal standards in various ways. For example, a captured government may tradeoff the benefits of stricter legal standards with the costs of their enforcement (Immordino and Pagano, 2003). However, a better picture of the market view on the impact of law 3016/2002 will emerge only after the whole set of responses is fully analyzed taking account additional factors, such as the size and activity of the company and the internal behavior of directors.

6. Epilogue: an effective corporate governance policy

Any recommendations on national policies relating to corporate governance must start by defining the core corporate governance problem facing a particular country, as these problems vary considerably. Effective corporate governance reform means a change in current governance practices. But this requires a careful understanding of the emergence of current corporate governance practices. The latter are largely a product of the regulatory systems put in place in each country and, for any given country, of their evolution over time, as well as of the institutional infrastructure within which these rules are applied. In practical terms, corporate governance reform must in general either take the rules and standards as given and focus on affecting the policy choices made by regulators and the state properly located within the prevailing institutional environment, or focus on the proper design of legal rules and standards assuming that policy makers generally seek to adopt optimal rules.

But the observed divergence in corporate governance practices and the effectiveness of their enforcement relates to innate, long-standing differences in legal origin, state politics, culture and ideology, even religion, all of which lie outside the realm of current policy making. However, given that policy makers do change their legal and regulatory arrangements considerably over time, the level of investor protection and efficient corporate governance at any given point in time may also result, at least partly, from current policy making. Hence, an explanation of the observed divergence in corporate governance and legal rules and their enforcement efficiency may be sought in the complex determination of public policy decisions. Such decisions on investor protection may be influenced and sometimes distorted by the activities of rent-seeking interest groups. There are several ways in which interest groups may capture policy-maker decisions or may conflict with each other, which have been studied by several political economy models. As a result of this complex interaction, relating to the structure of political and legal decision making, the developmental stage of the economy, the ownership and corporate structures dominant in the specific economy as well as to waves of corporate scandals and stock market crashes, the causality of the established positive correlation between legal rules, investor protection and good economic outcomes can go both directions: a high level of investor protection may be partly the result as much as the cause of a developed stock market, advanced economic performance of firms and a financially stable economy.

Thus, given the complexity of public policy decisions and the manner in which they are applied, efficient reform presupposes among other things that the strong insider influence of powerful interest groups with sufficient stakes and expertise can be effectively checked by brave public measures introduced by ethical and visionary policy makers aiming at safeguarding investor rights. Most corporate scandals of the recent past and the dire impact of the recent financial crisis provide the opportunity and the cause for investors and voters to be more attentive to corporate governance problems.

In the modern environment of international finance, efficient reform cannot but be guided by proper internationally accepted standards and, given national complexities, brave public measures can only be taken at the international level. Notwithstanding the need for improving and customizing international standards, the major failures among policy makers and corporations appear to be insufficient implementation of these recommendations. In this respect, I would agree with Lazaridis that the regulator's enforcement policy is a crucial factor in this respect. But, as this paper has argued, overall corporate governance enforcement efficiency is a much more complex issue whose understanding requires a most sophisticated institutional approach. The econometric results derived from a set of formal model equations in the law-and-finance tradition used by Lazaridis are unlikely to produce a comprehensive picture of corporate governance enforcement in Greece and should at least have been interpreted with due moderation and caution.

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