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Companies' Board Models and Their Influence over Company Performance and Corporate Governance Effectiveness

- Abstract -

In this paper we will put our focus on the operational board models in developed economies, while stressing their advantages and limitations. We continue our research to the new trends in shaping board structure and its effectiveness. Since our paper is primarily of a legal nature, we carry on with the issues related to the question as to what are the core directors' duties and liabilities, by whom and to whom these duties are owed, and what are the consequences for breaching these duties. Finally, we address the current situation in Macedonia regarding the topics covered in the paper.

Key words: corporate governance, board models, board composition, board effectiveness, board members' duties, liabilities and sanctions

Introduction

A quick web search can expose a number of various definitions of the term corporate governance (CG). One of the most widely used definitions is the one provided by the OECD, which reads that CG is "the system by which companies are directed and controlled"(Nerantzidis *et al,* 2012).

"In a nutshell, corporate governance arrangements are all about achieving the appropriate balance between the degree of commitment and control to different parties" (Mayer, 2012).

The major CG problem results from the lack of a precise definition of directors' duties as an alignment of decision making and the company's interest, or better regulation of the relationship between ownership, board structure and performance. Improvement of internal controls is the main focus of the current company law and CG reform processes (Hopt *et al,* 2004 and Nanka-Bruce, 2009).

The recent breakdown of the energy provider Enron, one of the largest publicly traded corporations in the U.S., has revealed major deficiencies in the United States', mainly market-based, CG system. This case revealed that all control mechanisms have failed (Hopt *et al,* 2004).

I. Board models

The corporate boards and their role have never been pressured and scrutinized as they are these days.

Comparatively, two basic board models can be differentiated in Europe: the two–tier board model and the one-tier board model.

Germany and the UK are paradigms of systems in which the control of managing directors of companies either lies in the hand of a separate supervisory board - SB (two-tier system), or is an additional task of the board itself (one-tier system) (Jungmann *et al,* 2006).

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Due to the different corporate governance models, the UK monistic board system results as a consequence in a market-oriented, externally (outsiders) based CG model, while the German board model is rooted on the block-holder, internally (insiders) based corporate governance approach (Moerland, 2005).

I.1. German Two-tier Board Model

German company law is the main representative of the quite rigid statutory regulated two-tier board models, i.e. the dualism of a management board and a separate SB. This system is also found in the Netherlands, Austria, Finland and Denmark (Hopt *et al,* 2004 and (Jungmann *et al,* 2006).

The central feature of internal corporate governance lies in the organizational and personal division of management, and control by a two-tier structure that is mandatory for all public corporations, regardless of size or listing.

While the clear responsibility of the management board (Vorstand) is the running of the business, the role of the SB (Aufsichtsrat) is not easy to describe. Its legal functions are primarily the appointment, oversight, and removal of members of the management board. On the other hand, SB members are appointed by the shareholders (Avilov *et al,* 1998).

The SB core task, however, is to supervise the management (not the corporation).

Consequently, in Germany, the members of the SB are the predominant monitors of the corporate management.

I.2. United Kingdom One-tier Board Model

In Europe, the UK is the major representative of the one-tier board model, known as "single board system". The term "board of directors" is used as a generic term to describe the institution that is elected by shareholders to supervise the management of the company (Avilov *et al,* 1998). The one-tier board model in the UK entrusts both management and control to the hands of the board of directors, who are vested with universal (same) powers. In larger companies, managerial power is delegated to groups of directors (committees) or individuals.

All board members, i.e. executive directors as well as non-executive directors are elected and removed from office by the shareholders. The single board manages the company.

The question arises as to how the role of an executive director differs from the role of a non-executive director? Non-executive directors are not employees of the company, but they are, as members of the board, concerned with managerial problems. Thus, the non-executive directors "should constructively challenge and help develop proposals on strategy" (Jungmann *et al,* 2006).

Another distinctive characteristic of the UK board model is the separation of the positions of board chairman and chief executive officer (CEO) as a functional distinction between control and management.

I.3. US Board Model

The US board model resembles the UK model. The traditional US model of corporate structure, the board of directors manages the corporation's business. Although boards generally continue to maintain this central legal role, it is the corporate executives who hold management functions, not the board members. The term "monitoring model" has been adopted to recognize that management functions are no longer exercised by the board, but are delegated to senior executives. However, the board of directors is the ultimate decision-making body and ultimately monitors the senior management in its day-to-day performance (SHU-ACQUAYE, 2011).

1.4. Criticisms for Both Models

Both basic board models, however, are subjected to criticisms.

The German model is criticized for being inflexible due to its mandatory statutory regime. In practice, the members of the SB are pre-selected by the management board and are only formally elected in the general meeting. In practice this results in a situation where the members of the SB are not completely independent when exercising control. The members of the SB, by definition, do not make strategic management decisions of their own. Instead, their role is limited to *ex post* evaluating measures already taken by the management board. The access of the members of the SB to sensitive information is limited (Jungmann *et al,* 2006). The information asymmetry on the side of the SB is significant due to the fact that the management transfers only the information that it relied upon itself. Business relationships (especially banks) and cross shareholdings are inherent characteristics of the German SB, and can involve difficult questions of independence, objectivity, and conflicts of interests.

For a long time the British model has been regarded as being superior to the German system. However, the single-board model has weaknesses as well: the members of the unitary board fulfill both managerial and supervisory functions. Thus, they face a dilemma: should they make decisions and, at the same time, monitor these decisions. The mere fact that there are executive and non-executive directors is not sufficient to guarantee the adequate execution of the monitoring role. The independent non-executive directors face the dilemma of being colleagues with the other board members while also having to monitor them at the same time.

What is recommended to remedy the weaknesses of both models?

As for the German model: SB membership should not be considered as a honorary position anymore; the role of the chairman should be strengthened by requiring this person to become a full-time job; the chairman should remain strictly independent; a chairman should not hold seats on other supervisory or management boards; the chairman should have unlimited access to all sources of information; the roles of the other members of the SB also need to become more professionalized; an adequate number of independent members of the SB should be reserved; introduction of mandatory qualification standards for SB members; diversity of experience and knowledge should be recognized; the SB should have more opportunity to exert influence on the decisions *ex ante,* etc.

What can be improved in the one-tier system?

The key to successful control of the management of the company is to reduce the potential conflict inherent in the monitor-colleague dilemma. This can primarily be done by choosing independent non-executive directors. The board should have meetings that would last several days as a way of better integrating and strengthening the position of the non-executive directors. By decreasing the number of directors, the more likely it is that each director can play an active and vital role and the free riding problem will be lessened (Nanka-Bruce, 2009).

1.5. Which board model should prevail?

The UK and Germany represent prototypes of two competing systems. Hence, the answer to the question whether it is possible different corporate governance models to converge would definitely be negative. Systems develop according to their historical and cultural background and according to the share-ownership structure and the capital market liquidity (path dependence).[2] Therefore, the often raised question as to whether one of the two systems will finally prevail, the answer has to be negative.

II. Board Composition, Independence, Effectiveness, Improvements

II.1. Board Composition and Independence

Policymakers in many countries have turned to independent (outside) directors as an important element of legal and policy reforms in the field of corporate governance. Independence is definitely one of the cornerstones for efficient control. This has been translated into many soft law acts (codes and best practice recommendations) requiring the introduction of a minimum percentage of independent directors both for the board as a whole as well as for some sub-committees (Vagliasindi, 2008).

The agency theory supporters claim that board outsiders are not entrenched and positively affect performance and control. On the other hand, it is documented that inside directors tend to make coalitions with the CEOs (Fu *et al*, 2010, Hill *et al*, 2012 and Vagliasindi, 2008).

One of the mechanisms to enhance the independence of the board members is the development of intra-board structures, such as task-specific committees. Although intra-board, these committees can be classified somewhere in the middle between inside and outside control. Task specific committees include the audit committee, the compensation committee, and the nominating committee should comprise a majority of independent directors. Each committee is functionally tasked in areas where the interests of managers and the shareholders or directors may conflict. However, the task-specific committees should not be allowed to take over resolution power in matters reserved for plenary decisions of the SB.

[2]There is a vast literature dealing with the path dependence and the possible functional and formal convergence of different corporate governance models. For example see: (Hertig, 2004,).

Further, in measuring board independence, it should be measured whether the CEO is involved in the selection process of board members and whether the CEO sits either on the board or in the nomination committee. The authors find that CEO involvement decreases the firm's number of independent directors (Vagliasindi, 2008).

II.2. Board Effectiveness

As we mentioned above, better firm performance is often identified with more outside directors. However, this inference appears not to be completely correct and mixed findings can be identified regarding this hypothesis in developed markets. While an outsider-dominated board alleviates the agency problem (but at the same time increases agency costs) between managers and shareholders, an insider-controlled board improves the efficiency of board decisions by better exploiting insiders' information (Fu *et al*, 2010).

Consequently, board outsiders will be expected to know less about the production process of a firm, especially when they operate in firms with different production technologies. (Nanka-Bruce, 2009).

De iure independence is an important parameter of board structure. On the other hand, some companies look for more firm-specific and generic expertise of directors (Biondi, *et al.*, 2005).

The SB made entirely of outsiders has a negative relationship with firm value. Outsiders are employed on the board on a part-time basis, and this limits their scope in understanding the complexities involved in taking informed decisions (Nanka-Bruce, 2009, Bhagat and Black, 1999).

Another important aspect in measuring board effectiveness is the CEO-chairman separation. CEO-board separation indicates how independent a board is, since the CEO who is also the chairman of the board exercises too much control that can promote abuse of power. However, both CEO-chairman duality and separation do not substantively differ in both their effect on financial performance, and on firm's profitability (Nanka-Bruce, 2009).

Regarding the CEO's role, it should be noted that a number of studies have documented a positive relationship between CEO pay and poor performance (Vagliasindi, 2008).

II.3. Board Performance Improvement

II.3.1. Executive Remuneration System

One of the most publicly debated developments in corporate governance has been the explosion of executive compensation. Hence, in many countries around the world the ability of the board to effectively monitor executive remuneration, appears to be a key challenge in practice and remains one of the central elements of the corporate governance debate. Generally, hard law tools seem that are quite limited to influence remuneration. Thus, many jurisdictions have favored soft law measures that can go further in providing guidance on the structure of remuneration systems (Hill *et al*, 2012 and OECD, 2011).

There are two basic positions. The first one believes that equity, share-based compensation represents an efficient approach to align the incentives of corporate officers with the longer term interests of shareholders by introducing, at the same time, better oversight by the board. On the other hand, where share-based remuneration forms a significant part of total remuneration, it could lead to overly risk-averse management (Fisch, *et al*., 2003).

The other holds that increased compensation is a sign that officers have captured boards (Vagliasindi, 2008 and Hill *et al*, 2012).

The "say-on-pay" approach within corporate governance should be mentioned in this respect. That would let shareholders have an active and informed vote in determining how companies pay their top executives, thus gaining sufficient capacity to influence the board (Gordon *et al*, 2009, Ferri, *et al*. 2011 and Cheffins, *et al*,. 2001).

In jurisdictions (Sweden, Brazil), in which controlling shareholders are more common, the remuneration structures are less aggressive. In the same jurisdictions, the general meeting assumes direct control of the remuneration setting process, and the role of the board is limited to implementing the shareholders policies. In contrast, in the UK the average compensation package of CEOs has risen significantly over the past ten years (OECD 2011).

II.3.2. Board Members Selection

The process of selection and appointment of board members, through structured and skill based nomination process should be strengthened. A database of qualified candidates can also be considered to help enlarging the pool of potential experts for boards. In addition, the director selection process should be modified by incorporating greater shareholder input, which would enlarge director accountability to shareholders (Fisch, *et al*., 2003 and Vagliasindi, 2008).

II.3.3. Board Members Training and Evaluation

Another important aspect is that board members and executives should continuously be trained (capacity building) about their duties and liabilities in governance changes context.

The assessment of board performance is the next essential matter for demonstrating accountability and generating public trust. Board evaluation is necessary to identify existing mix of competences and skills, and specify new profiling for new Board positions. This board evaluation should demonstrate how well the board has performed against any performance objectives set. Regular use of an external facilitator (e.g. every third year) could improve board evaluations by bringing an objective perspective and sharing best practices from other companies (Vagliasindi, 2008).

Some authors promote the idea that individual directors should self-certify their independence. (Low, 2004).

In relation to board evaluation we would like to mention the Slovenian case. The Slovenian Directors' Association introduced in 2011 the SB Assessment Manual and the SB self-Assessment Matrix.[3]

[3] http://www.zdruzenje-ns.si/zcnsweb/default.asp

II.3.4. Gatekeepers

There are some examples where the financial regulator (the US Securities and Exchange Commission), within its authority to promulgate professional standards of conduct, promotes a new corporate governance structure - the qualified legal compliance committee (QLCC). In accordance with this idea, the QLCC should reduce the statutory emphasis on lawyers as gatekeepers in favor of increasing the focus on board structure and director independence. The opponents of this idea identify that the introduction of these specialized board committees and mandating standards of independence may, by itself, be insufficient to address a widespread problem of director passivity (Fisch, *et al.*, 2003).

Another trend in both corporate governance and corporate law has been a growing focus of the role of the variety of gatekeepers. These are professionals who act as informational and reputational intermediaries. They gather information about companies, and help to warrant to outsiders the validity of the publicly available information. Important gatekeepers include corporate lawyers, rating agencies, auditors and accountants, securities analysts, D & O insurers, investment banks, etc., although some of these gatekeepers (rating agencies) were strongly criticized for their poor performance during the financial crisis (Hill *et al*, 2012 and Blaurok 2007).

III. Duties and Liabilities of Directors and Officers

When making general assessment of company law and the corporate governance environment in one country, the emphasis should be put on directors' duties and liabilities (Black et al., 2008 and Mathias *et al*,, 2000, Coelho, 2007).

III.1. What are the Core Directors' Duties?

The directors are granted with authority to direct corporation's affairs. However, in the modern corporation, directors delegate their management power to senior officers. Although such delegation is proper, directors are expected to oversee the conduct of senior officers. Because directors have the legal power, they also bear the burden of exercising such power responsibly. The core duties of directors consist of two basic functions: decision-making and oversight. "The tradeoff between authority and accountability is at the heart of corporate law" (Jones *et al,* 2012 and SHU-ACQUAYE, 2011).

Corporate law should specify standards of conduct for members of the board of directors and the members of other management organs. These directors' duties are governed by an objective "reasonable person" legal standard in the field of care and skill, and an objective test is applied in imposing liability in regard to a breach of their duties (Jones *et al*, 2012, Hopt *et al*, 2004 and Avilov *et al,* 1998).

The directors' duties can be comparatively analyzed within the common law and the civil law context.

Under common law, corporate law imposes fiduciary duties of loyalty and care on directors. The duty of loyalty prohibits self-dealing and the taking of business opportunities away from the corporation for the personal benefit of the director. The duty of care requires directors to exercise the degree of care that an “ordinarily careful and prudent men would use in similar circumstances” (Black et al., 2008).

Fiduciary relationships are by their very nature relationships of good faith. This duty, however, is directly related to conflict of interest doctrine. Namely, the director is violating his duty of good faith by engaging in transaction which involves a direct or indirect conflict of interest without appropriate disclosure and approval by non-conflicted members of the board or the shareholders (as the case may be) in mandatory procedures required by law. A person has a conflict of interest if that person will realize a financial or other advantage from a transaction with the corporation. In some jurisdictions (Germany) a requirement that directors act in good faith is not covered by the company law. Instead, the general civil law requirement of good faith for parties to a contract applies (Black et al., 2008).

The civil law requirement of reasonableness and the rules that establish liability of directors for negligence can be compared with the common law duty of loyalty. As we mentioned, fiduciary relationships may involve a variety of obligations. In continuation we will mention some of them: the duty of reasonableness; the duty of disclosure; the duty of confidentiality; the due diligence duty; the duty to return preference payments and duty to prevent tunneling activities (Hill *et al*, 2012); the duty in insolvency - liability on directors for allowing the company to continue its operations, without filing for insolvency, when it has become insolvent; etc.

III.1.1. Business Judgment Rule

In evaluating fiduciary duties, courts in fact examine compliance with these duties by using the "business judgment rule," which presumes that the board decisions were made on an informed basis, in good faith, and in the best interests of the corporation. In absence of discretionary abuse of directors’ fiduciary duties, the business judgment rule will prevail and not be second guessed by the courts. The justification usually articulated for the business judgment rule is that without it people would not be willing to serve as directors, or take appropriate risks for the benefit of the corporation (SHU-ACQUAYE, 2011).

III.2. Equal Position in Discharging Duties

In discharging their duties, it is recommended that directors should have equal positions. Different standards of liability for different directors, depending on their positions, or on whether they serve on particular committees of the board of directors are not supported.

However, the outside directors should be exempted from this doctrinal approach. If litigation against outside directors represents a significant risk, then outside directors will be reluctant to serve. The ratio of reward (the modest compensation that is customarily paid) to risk (the potential for being found liable for very large damages) will simply be unacceptable. A second possibility is to limit the amount of monetary liability that outside directors face if they adopt decisions in a situation not involving a conflict of interest (Black et al., 2008).

III.3. Should Directors' Duties be Extended to Other Persons?

A question that arises is whether directors' duties should also apply to senior managers and other involved "interested" parties? In comparative literature it is recommended these duties not apply only to the directors, but their relevance be also extended to members of formal management bodies, such as officers, managing organizations, controlling shareholders, the so called "shadow" or *de facto* director, the parent company (but only in limited circumstances) etc. (Black et al., 2008).

There are also recent trends of imposing civil liability on auditors are owed directly to shareholders.[4]

III.4. To Whom Does a Director Owe a Fiduciary Duty?

With respect to the answer of this question two things should be differentiated: first, the fiduciary duties owed to solvent company and second, fiduciary duties owed to insolvent companies or when company is entering the "zone of insolvency".

Hence, the issue as to whom fiduciary duties are owed can be analyzed from the prospective of various economic stages of the corporation (BACHNER, 2009 and SHU-ACQUAYE, 2011).

While the company is solvent, the position is quite clear. When a company is financially healthy, the directors owe fiduciary duties to the corporation and its shareholders.

Things become much more blurred when a company is nearing insolvency, or is already insolvent. In the case of corporations entering the zone of insolvency, some scholars and courts in the US for a quite a long time held the position that fiduciary duties are owed to creditors in addition to the corporation and shareholders.

However, in the decision of *North American Catholic Educational Programming Foundation, Inc. v. Gheewalla* (No. 521, 2006) (Del. May 18, 2007), the Delaware Supreme Court for the first time expressly rejected the existence of a cause of action by a creditor against a corporation's directors for breach of their fiduciary duties to the creditor where the corporation was insolvent or in the "zone of insolvency."

III.5. Breach of Fiduciary Duty

As we already mentioned above, persons in a position of trust or fiduciary relationship, such as directors, managers or officers owe certain fiduciary duties.

A breach of fiduciary duty claim is a civil action. However, before the court can order the payment of damage compensation, it must be satisfied that a breach of duty has occurred and that the corporation has suffered damage as a result of that breach (Jones *et al*, 2012).

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[4] A study on systems of civil liability of statutory auditors in the context of a Single Market for auditing services in the European Union, available at http://ec.europa.eu/internal_market/auditing/docs/liability/auditliability_en.pdf

III.5. Liability and Remedies for Breaching Director's Duties

For breaching the fiduciary duties the directors can be found liable for damages caused to the company under the general civil law regime. Civil liability compensates the aggrieved party for all losses it has borne - both actual losses and lost profit.

However, additional remedies may be available. With specific regard to conflict-of-interest transactions, voidability of the transaction is also a common remedy.

The same damage remedies should be available for a breach of duty owed to the company by other persons, including members of the company's executive organ, senior managers, officers, shadow directors and controlling shareholders. (Black et al., 2008)

The very common sanction for breaching the director's duty is the disqualification of directors and managers, for a period of time from serving as a director or manager of a company, based on serious breach of duty. The disqualification may be followed by a shareholder suit seeking damages.

Apart from civil liability for breaching fiduciary duties, directors can be found liable under securities law, banking law, administrative law, insolvency law, criminal law, competition law, environmental law, and so on.

However, in comparative law there is strong recommendation for there not to be administrative penalties for breach of duty owed to the company under company law.

In some jurisdictions there is criminal liability provided for at least some violations of company law. This creates the potential for criminal enforcement by the prosecutor. The commentators often criticize the prosecution for bringing inappropriate cases just for political advantage and thus, the prosecutors have been criticized for potential misuse of their powers.

III.6. Compensation for Damages Caused by Directors

The most significant barrier to director liability for oversight failures are exculpatory provisions adopted in many countries that immunize directors from liability (Jones *et al*, 2012).

Due to the frequency of exculpatory provisions in corporate charters, a director's failure to provide proper oversight will often not result in personal liability.[5]

The business judgment rule offers directors an initial layer of protection from personal liability. Thus, directors will not be held to account for ill-advised decisions, so long as a rational basis for the decision can be found (Jones *et al*, 2012).[6]

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[5] For example, IN RE CAREMARK INTERNATIONAL INC. DERIVATIVE LITIGATION CONSOLIDATED CIVIL ACTION NO. 13670 698 A.2d 959, 1996 Del. Ch. LEXIS 125 (Del. Sept. 25, 1996) {960} the court concluded that no breach of duty had likely occurred, as the board had adopted a compliance program that nonetheless failed to prevent the legal violations. Jones, Renee M. and Welsh

[6] There are, however, circumstances in which directors are not entitled to the presumption afforded by the business judgment rule. Among other things,

Under US business practice, it is important to distinguish between compensation for damages, or for civil or criminal penalties, and compensation for legal and other expenses. (Black et al., 2008).

It is strongly recommended that compensation against administrative or criminal penalties should not be permitted.

In contrast to common practice in the United States, Australian corporations are prohibited from exempting directors from liability for pecuniary penalty and compensation orders imposed under the civil penalty regime.

III.6.1. Directors and Officers (D&O) Insurance

The comparative debate suggests that even countries which restrict the ability of companies to compensate directors for damages paid in a civil suit generally allow companies to purchase Directors and Officers (D&O) insurance, which may provide means for corporations to limit the substantive exposure of directors to liability. Damages in a civil suit should generally be insurable with exception to director's personal financial benefit; damages that result from an intentional violation of law by the director or manager; administrative or criminal fines and penalties; etc.

III.7. How the Directors' Duties Can Be Enforced?

Usually, the question arises as to who has the power to enforce the directors' liability, from the civil law prospective?

Since the directors owe fiduciary duties to the corporation and its shareholders, shareholders can bring direct or derivative claims against directors.

Direct action is a suit by shareholder in his own right to redress any harm suffered directly by him for which he is entitled to personal relief. A direct suit brought by shareholder usually includes actions to recover dividends and to examine corporate books and records.

When a corporation is unwilling to sue the director for breaching his duties a derivative suit can be brought by shareholders in the name of and behalf of the company, seeking to enforce directors' duties to the company. This is due to the fact that the board members or the SB are reluctant to bring action, because its members must fear liability for failure in the exercise of control over management (Hopt *et al*, 2004, Avilov *et al*, 1998 and J.B., 1962).

Should any other actor or institution be entitled to trigger directors' civil liability?

The comparative experience shows that the regulator of financial markets usually does not have the power to enforce the statutory civil law duties of corporate directors (Black et al., 2008).

Also, financial regulators should not have power to seek criminal proceedings.

The regulator may have investigative power, but just to be commensurate with the scope of its statutory authorizations, and limited only to public companies.

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this will be when a director has a personal interest in a matter, implicating the duty of loyalty.

Whatever the case may be, it is recommended to avoid overlapping and concurrent authorizations of different public and private actors to trigger remedies for company law violations, as much as possible.

Finally, is should be stressed that there are significant practical difficulties in establishing directors' liability. Namely, there are important procedural obstacles, which make it difficult in practice for shareholders to bring a suit against a company's directors and officers (Mathias *et al*,, 2000, Hill *et al*, 2012 and Jones *et al*, 2012).

IV. The Country Case of the Republic of Macedonia

Macedonian company law and corporate governance framework consists of few hard and soft law normative acts: the 2004 Company Law (CL) with the subsequent amendments; the 2005 Securities Law with the subsequent amendments; the 2006 Corporate Governance Code for Companies Listed on the Macedonian Stock Exchange, which on itself is based on the 2004 OECD Principles of Corporate Governance and the Decision on the Basic Principles of Corporate Governance in a Bank.[7]

The 2004 Company Law mainly results from the transposition of the EC Company law directives with their subsequent amendments.[8] In its essence, this Law follows the German company law tradition, with exception of German labor co-determination.

The 2006 Corporate Governance Code for Companies Listed on the Macedonian Stock Exchange is currently under process of revision due to the ongoing European debate regarding possible changes in corporate governance environment (Green Paper, 2011 and Andersen, 2011).

2009 saw the birth of the Macedonian Institute of Directors (MIoD) - a non-governmental organization which is dedicated to creating a positive impact on the economy and society by promoting professional directorship and good governance. The focus of their

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[7] Enacted by the Council of the National Bank of the Republic of Macedonia and published in the Official Gazette of the Republic of Macedonia no. 159/2007.

[8] In this occasion we would like to refer to some directives that significantly influenced the amending process into Macedonian legislation: DIRECTVE 2006/43/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/ 660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC; Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies (OJ L 184, 14.7.2007, p.17–24). In addition to this, some recommendations are taken into consideration, although not yet transposed into the hard law acts: Commission Recommendation 2005/162/EC of 15 February 2005 on the role of nonexecutive or supervisory directors of listed companies and on the committees of the (supervisory) board (OJ L 52, 25.2.2005, p. 51–63); Commission Recommendation 2004/913/EC of 14 December 2004 fostering an appropriate regime for the remuneration of directors of listed companies (OJ L 385, 29.12.2004, p. 55–59); Commission Recommendation 2009/385/EC of 30 April 2009 complementing Recommendations 2004/913/EC and 2005/162/EC as regards the regime for the remuneration of directors of listed companies (OJ L 120, 15.5.2009, p. 28–31).

activities is put on supporting boards of directors and supervisory boards to add value to their strategic decisions. MIoD is an affiliated member of European Confederation of Directors' Associations (ecoDa) since July 2012.

Two editions on the Corporate Governance manual for Macedonian Stock Companies were published in 2007 and 2011 on partnership basis between IFC, USAID Macedonia, the Swiss State Secretariat for Economic Affairs (SECO), the Macedonian Stock Exchange and the MIoD.

The overall impression is that Macedonian company law and corporate governance framework incorporates a variety of international good governance practices.

However, there is no precise definition under Macedonian law as regards to division between public and private joint stock companies (JSCs). Instead, a term "joint stock company with special reporting requirements" is used for public companies. By this term JSCs that have (a) either made a public offering of securities, or (b) that have a basic capital of 1.000.000 euro in Denar value and more than 50 shareholders or (c) that are listed on the stock exchange are covered.

Two joint stock companies are on super listing, while 30 are on exchange listing on the official market on the Macedonian Stock Exchange. The application of Macedonian Corporate Governance Code is mandatory for the JSCs on super listing on "comply-or-explain" basis, while for the JSCs on exchange listing its application is on a voluntary basis.

Macedonian JSCs have the option of choosing one-tier or two-tier boards. Under the two-tier system, there is a supervisory board and a management board. The function of company secretary (compliance officer) does not exist in law (with exception to the banking and insurance sector). According to the data available on the Macedonian Stock Exchange (www.mse.mk) eighteen JSCs selected the two-tier model, while fourteen opted for one-tier (single) board model.

Due to the limited scope of this paper, in continuation we would not like to replicate what was already elaborated in the previous sections. Instead we would like to refer to the (ROSC) Report on the Observance of Standards and Codes (ROSC), Corporate Governance, Country Assessment Former Yugoslav Republic of Macedonia, The World Bank, June 2005, since there are not much substantial changes as to the findings documented in this Report regarding topics confined in the paper.

Conclusion

It is hard to say that outsider directors, non-executive directors, independent directors or competent, well paid, full-time working members of the (supervisory) board have a degree of foresight that makes them, in any case, superior to the executive directors or members of the management board. Both groups can be wrong in their decisions; both might take too many risks and thus lead the company into a period of financial distress. Thus, neither integrating the monitors into the decision-making process, nor strengthening the role of those involved in the decision-making process as monitors would automatically bring to an end the business failures (Jungmann *et al,* 2006).

Provided that minimum set of mandatory rules is kept, it seems most promising to leave the detailed definition of adequate board balance between mere non-executive independence and higher standards of independence to the discretion of the individual company.

Thus, contrary to the popular view, a lot of studies have shown that governance is not "one-size-fits-all" and applying one-size-fits-all criteria on a corporate board can be costly and inefficient to some firms (Fu *et al*, 2010 and Skog, 2012).

Even more, optimal board structure by some authors is deemed as one of the corporate governance myths, despite the lack of strong supporting evidence (Larcker *et al*, 2011).

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