Comparative Corporate Governance: Irish, American, and European Responses to Corporate Scandals

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I. Introduction

The late 1990s were good for worldwide business. Stock markets were exuberant, multinationals were selling to the far corners of the planet, and the world was more or less at peace. But like the month of March, the 20th century ended like a lamb and the 21st started like a lion. The 2000 American presidential election proved to be an affair more complex than simply counting votes, September 11, 2001 became a date forever etched in my generation's mind, and in November 2001 the fifth-largest[1] American company, Enron, went bankrupt. In lemming-like fashion, companies around the world followed Enron in revealing scandalous corporate and accounting policies.

Just as turn of the century events sent President George W. Bush to war with Afghanistan and Iraq, Senator Paul Sarbanes and Congressman Michael Oxley went to war against bad corporate practices. Their product, the Sarbanes-Oxley Act of 2002 (SOX), became the standard-bearer for how government would regulate business. The Irish and the European[2] responses to scandals mirror SOX.

This paper reviews and comments upon how the American, Irish, and European governments responded to this millennium's corporate scandals. Part II reviews the roots and effects of corporate scandals. Part III digresses slightly from the main purpose by introducing the basics of Irish and European corporate law. This introduction is included to facilitate understanding of Part IV, which reviews recent American and Irish corporate governance legislation and European Union (E.U.) regulations, directives, and proposals. Part V compares and contrasts these government responses. It concludes that the Irish legislative response was out of proportion to Irish scandals, but that it fits into a greater mold of convergence in which the

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[1] Enron ranked 5 on the 2002 Fortune 500 list. *See* http://www.fortune.com/fortune/fortune500/articles/0,15114,373322,00.html (Last visited Nov. 23, 2005).
[2] When I use "European" or "Europeans" I am referring to the European Union (E.U.).

U.S provides the model for corporate governance and the E.U. acts as a competent body to facilitate convergence of diverse corporate practices.

II. Scandals

American accounting scandals are well known on both sides of the Atlantic.[3] Not known to most Americans (or even to much of the Irish and European public) are the instances of corporate malfeasance on the eastern side of the Atlantic. This section reviews the major corporate and accounting scandals that served as catalysts for the governmental action which is reviewed in Part IV.

A. American Scandals

Enron & Arthur Andersen

Enron hid assets and liabilities in over 2,000 businesses, many of which where wholly-owned special purpose entities (SPEs) that were not included on the Houston energy trader's financial statements.[4] Enron booked loans as revenue and often sold that debt to its SPEs, again recording revenue from the sale.[5] In November 2001, Enron restated earnings and debt for the years 1997-2000. It reduced earnings by $28 million for 1997, $133 million for 1998, $153 million for 1999, and $91 million for 2000. It increased debt (by returning liabilities held in SPEs back to its own balance sheet) by $711 million for 1997, $561 million for 1998, $685 million for

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[3] *See e.g*. Roberta Romano, The Sarbanes-Oxley Act and the Making of Quack Corporate Governance, 114 Yale L.J. 1521, 1528 (2005); John Paul Lucci, Enron – the Bankruptcy Heard Round the World and the International Ricochet of Sarbanes-Oxley, 67 Alb. L. Rev. 211 (2003); Marianne M. Jennings, Primer on Enron: Lessons From A [sic] Perfect Storm of Financial Reporting, Corporate Governance and Ethical Culture Failures, 39 Ca. W. L. Rev. 163 (2003); Robert W. Hamilton, Seventh Annual Frankel Lecture Address: The Crisis in Corporate Governance: 2002 Style, 40 Hous. L. Rev. 1 (2003); Luca Enriques, Bad Apples, Bad Oranges: A Comment from Old Europe on Post-Enron Corporate Governance Reforms, 38 Wake Forest L. Rev. 911 (2003); Communication from the Commission to the Council and the European Parliament -- Modernising Company Law and Enhancing Corporate Governance in the European Union -- A Plan to Move Forward, COM (2003) 284 final (May 2003), p.5 ("The Sarbanes-Oxley Act, adopted on 30 July 2002 *in the wave of a series of scandals…*" [emphasis added]);

[4] Hamilton, *supra* note 4, at 8-9.

[5] Id. at 9.

1999, and $628 million for 2000.[6] "Nearly a third of Enron's reported income came from misclassification of transactions as revenues."[7] Even before Enron's bankruptcy, its auditor, Arthur Andersen, LLP (Andersen), classified it "as a 'maximum risk' client - meaning that it adopted and used the most aggressive permissible accounting principles."[8]

Andersen had a number of conflicts of interest in its Enron account: it generated more revenue from providing consulting services ($27 million) than it did from providing auditing services ($25 million); the "staffs of Enron and Andersen were inextricably intertwined;"[9] and Andersen was Enron's internal and external auditor.[10] Such was the conflict that Andersen was convicted of obstruction of justice for shredding Enron-related documents.[11] Andersen ceased to be an auditor of public companies on September 1, 2002 and shut down completely soon after.[12]

WorldCom

Ashburn, Virginia-based telecom giant WorldCom, Inc. (WorldCom) restated earnings downward by $3.8 billion in June 2002. It had booked expenses as capital investments, thus turning an expenditure of cash into a capital asset.[13] The company that emerged from bankruptcy had a market capitalization of less than $1 billion from a high of $115 billion.[14] It also changed its name to MCI.

Andersen audited WorldCom.[15]

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[6] Cherie J. Owen, Board Games: Germany's Monopoly on the Two-Tier System of Corporate Governance and Why Post-Enron United States Would Benefit From its Adoption, 22 Pa. St. Int'l L. Rev. 167, 170 (2003).
[7] Hamilton, *supra* note 4, at 12.
[8] Id. at 8.
[9] Jennings, *supra* note 4, at 213.
[10] Id. at 214.
[11] Hamilton, *supra* note 4, at 8.
[12] Jonathan D. Glater, Last Task at Andersen: Turning Out the Lights, N.Y. Times, at C3, Aug. 30, 2002.
[13] Hamilton, *supra* note 4, at 21.
[14] Owen, *supra* note 7, at 170.
[15] Hamilton, *supra* note 4, at 22.

Qwest

Qwest Communications International (Qwest), the dominant local phone company in fourteen states from Minnesota to Washington, improperly listed $1.16 billion as current profits rather than capital investments. While making its restatement on July 28, 2002, it wrote off $20-$30 billion in intangible assets.[16]

Andersen audited Qwest.[17]

Global Crossing

Global Crossing built an underwater fiber optic network that connected continents via the internet. When traffic did not pan out as expected, Global Crossing engaged in a scheme of "swapping" capacity with other telecommunications companies such as Qwest and recording the transactions as earnings. The company filed for bankruptcy in January 2002.[18]

Andersen audited Global Crossing.[19]

Adelphia

In March of 2002, Adelphia Communications disclosed that it had made loans worth $2.3 billion to its controlling shareholders, the Rigas family, without recording the transactions on its balance sheet. In June 2002, the company announced that it had $500 million less in revenue than it had reported over the previous two years. The company filed for Chapter 11 bankruptcy, listing $18.6 billion in debt. Its stock price fell to $.01.[20]

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[16] Id. at 24.
[17] Jennings, *supra* note 4, at 215.
[18] Jennifer S. Recine, Examination of the White Collar Crime Penalty Enhancements in the Sarbanes-Oxley Act, 39 Am. Crim. L. Rev. 1535, 1540-1541 (2002).
[19] Jennings, *supra* note 4, at 215.
[20] Owen, *supra* note 7, at 171; Hamilton, *supra* note 4, at 23-25.

Tyco

Tyco International lost $100 billion in market capitalization when its CEO Dennis Kozlowski was indicted on charges of New York state sales tax evasion.[21] Kozlowski used company money as his own, spending lavishly for personal expenses and at one point receiving a loan for $19 million which the Tyco board forgave without shareholder knowledge. The company recorded a loss of $2.32 billion in 2002.[22]

ImClone and Martha Stewart

ImClone Systems (ImClone) CEO Samuel Waksal learned on December 25, 2001 that the Food and Drug Administration (FDA) planned to reject ImCone's application for approval of a cancer drug. One day later, Waksal, his family, and friends began selling ImClone shares. Two days later, on December 28, 2001, ImClone publicly announced the FDA rejection and its share price dropped from $70 to $10. Waksal and friends saved $9 million by selling ImClone shares two days before the public announcement.[23]

Waksal was caught and pleaded guilty to insider trading.[24] One of his friends, lifestyle doyenne Martha Stewart, was convicted of obstruction of justice for lying to authorities about her sale of ImClone stock. She served five months in prison.[25] Within 30 minutes of her conviction the share price of Martha Stewart Living Omnimedia dropped from $17 to $10.86 and Stewart had paper losses of $186 million.[26]

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[21] Hamilton, *supra* note 4, at 26.
[22] Id. at 27.
[23] Id. at 28-29.
[24] Id. at 29.
[25] David Glovin, Judge Refuses to Cut Stewart's Detention, Wash. Post, at E01, Apr. 12, 2005.
[26] Neil Irwin, For the Stewart Brand, an Uncertain Future, Wash. Post, at A04, Mar. 8, 2004.

B. Irish Scandals

Elan

Elan Corporation (Elan) is an Irish pharmaceutical company headquartered in New York. Its common stock trades on the Irish Stock Exchange and its American Depository Receipts (ADRs) trade on the New York Stock Exchange (NYSE).[27] In its 2002 annual report, Elan reduced its 2001 reported income by $73 million and its cash flow by $500 million.[28] Elan's market capitalization fell from $20 billion in June 2001 to $600 million in July 2002.[29] Plaintiffs in a 2004 Elan securities litigation suit estimated that Elan inflated profits by $648.8 million.[30]

Elan engaged in an accounting practice called "roundtripping" whereby Elan provided loans to third parties which the third parties then returned to Elan soon after. Elan recorded the loans as capital investments and booked the return as revenue.[31] Elan's roundtripping schemes came in four flavors: joint business ventures (JBVs), a product rationalization program, risk sharing arrangements, and SPEs.[32]

Elan inflated sales income by entering into JBVs with other firms. Elan contributed money to the JBV which the JBV then used to purchase a license from Elan for medical technology. Elan recorded the purchase of the license as income. Elan also shifted its substantial research and development expenses to JBVs.[33]

In its product rationalization program, Elan sold royalty rights to other companies. The other companies paid for these rights with funds provided by Elan. Elan recognized income from the sale of royalties but did not record the expense of financing the transaction. Elan also

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[27] In re Elan Corp. Sec. Lit., 2004 U.S. Dist LEXIS 9913, 4 (S.D.N.Y. 2004)[Elan].
[28] Id. at 3.
[29] Shame About the Name, Economist, Jul. 13, 2002.
[30] Elan, 2004 U.S. Dist LEXIS 9913, 14.
[31] Id. at 6.
[32] Id. at 6-7.
[33] Id. at 7-9.

recognized the entire income from the sale in the year the sale took place rather than spreading the income over the length of the royalty contract.[34]

In its risk sharing arrangements, Elan financed its research and development by selling royalty rights to products under development. Elan characterized the money it received as sales when in fact they were reimbursements for research and development costs already incurred.[35]

Elan sold securities in JBVs to three SPEs at great profit. The SPEs did not have cash to buy the securities; they recorded debt for the purchases. Elan recorded profit on the sale, even though it never received cash. In 2000 and 2001, Elan recorded gains of $40 million on the sale of securities to SPEs. Elan guaranteed the SPE debt, but did not record the guarantees as debt on its own balance sheet.[36]

In addition to roundtripping, Elan had an ingenious compensation scheme that enriched executives to the tune of $20 million. Elan paid "royalties" to a company called Monksland. Monksland distributed its good fortune to its shareholders, all of whom were Elan executives. As such, Elan conveyed money to executives without disclosing the compensation to shareholders.[37]

Allied Irish Banks

Allied Irish Banks (AIB) is an Irish banking conglomerate with shares quoted on the Irish and London stock exchanges and ADRs quoted on the NYSE.[38] At Allfirst Bank (Allfirst), a wholly owned subsidiary located in Maryland, a rogue currency trader named John M. Rusnak

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[34] Id. at 9-10. Elan's income recognition scheme violated SEC Staff Accounting Bulletin 101. *See* Id. at 9.
[35] Id. at 10.
[36] Id. 12-13.
[37] Id. at 13-14.
[38] *See* http://www.aib.ie/servlet/ContentServer?pagename=AIB_Investor_Relations/Miscellaneous/ir_article_printer&c=AIB_Article&cid=1096576937320&channel=IRHP (last visited Nov. 18, 2005).

(Rusnak) caused Allfirst to restate earnings downward by $691 million.[39] A report commissioned by AIB found:

> The fraud was carefully planned and meticulously implemented by Mr Rusnak, extended over a lengthy period of time, and involved falsification of key bank records and documents.
>
> Mr Rusnak circumvented the controls that were intended to prevent any such fraud by manipulating the weak control environment in Allfirst's treasury; notably, he found ways of circumventing changes in control procedures throughout the period of his fraud.
>
> Mr Rusnak's trading activities did not receive the careful scrutiny that they deserved; the Allfirst treasurer and his treasury funds manager - the principal persons responsible for Mr Rusnak's supervision - failed for an extended period to monitor Mr Rusnak's trading.
>
> At both the AIB Group and Allfirst levels, the Asset and Liability Committees ("ALCOs"), risk managers, senior management and Allfirst internal auditors, all did not appreciate the risks associated with Mr. Rusnak's hedge-fund style of foreign exchange trading; even in the absence of any sign of fraudulent conduct, the mere scope of Mr Rusnak's trading activities and the size of the positions he was taking warranted a much closer risk-management review.
>
> Allfirst and AIB senior management heavily relied upon the Allfirst treasurer, given the treasurer's extensive experience with treasury functions and foreign exchange trading in particular. In hindsight, this heavy reliance proved misplaced.
>
> Nothing has come to attention during the course of the review that indicates that anyone at AIB or Allfirst, outside of the Allfirst treasury group, were involved in, or had any knowledge that, fraudulent or improper trading activity was occurring at Allfirst before the discovery of the fraud.[40]

An AIB ADR-holder, Tomran, Inc. (Tomran), filed a derivative suit alleging that AIB and Allfirst directors "were negligent and grossly negligent in their oversight of Rusnak, which resulted in the loss to Allfirst Bank."[41] Tomran sought money damages and declaratory and injunctive relief.[42] The Maryland Court of Special Appeals dismissed the suit, holding that under

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[39] Tomran, Inc. v. Passano, 862 A.2d 453, 455 (Md. App. 2004)[Tomran].

[40] AIB and Allfirst Implement Actions to Address Issues Raised by Fraudulent Trading Activities, March 14, 2002. Available at http://www.aib.ie/servlet/ContentServer?pagename=AIB_Investor_Relations/AIB_Press_Releas/aib_d_press_releases&c=AIB_Press_Releas&cid=1015597171590&channel=HP (last visited Nov. 18, 2005).

[41] Tomran, 862 A.2d at 456. An appeal is pending before the Maryland Court of Appeals. *See* Tomran, Inc. v. Passano, 872 A.2d 46 (Md. 2005) (granting plaintiffs' petition for a writ of certiorari).

[42] Tomran, 862 A.2d at 455.

Irish law a shareholder has no standing to enforce a right of the corporation via a derivative suit. In Ireland, derivative suits are "uncommon and difficult to sustain."[43]

Rusnak pleaded guilty to bank fraud and received a 7½ year prison sentence.[44] He must repay $691 million to Allfirst in $1,000/month increments. At that rate, his debt will be repaid in 57,583 years.[45]

C. European Scandals

Royal Ahold

Dutch food retailer Royal Ahold N.V. (Ahold) has been described as "Europe's Enron."[46] Ahold ADRs trade on the NYSE and its common stock trades on exchanges in Amsterdam, Brussels, Paris, and Zurich.[47] "Like many American firms during the bubble years, Ahold started to bend the accounting rules, claiming profits of acquired firms as 'organic growth', booking capital gains from sale-and-leaseback deals as profit, and keeping billions in debt off its balance sheet."[48] In February 2003, Ahold announced it was restating earnings downward by $500 million because of accounting inaccuracies at an American subsidiary, U.S. Foodservice, Inc. (USF). Ahold's stock price dropped more than 60%.[49] Ahold had 2002 losses of $1.4 billion and in 2003 wrote off $3.1 billion in debt related to USF.[50] Two accounting practices in particular caused most of Ahold's problems: improperly booking income from vendor rebates and inflating revenue from joint ventures.[51] USF prematurely booked vendor rebate revenue and colluded with

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43 Id. at 466.
44 Ex-Currency Trader Sentenced to Seven and a Half Years, N.Y. Times, Jan. 18, 2003.
45 57,583, Wash. Post, at E02, Jan. 20, 2003.
46 Europe's Enron, Economist, Mar. 1, 2003.
47 In re Royal Ahold N.V. Sec. & ERISA Lit., 351 F. Supp. 2d 334, 348 (Md. 2004)[Royal Ahold].
48 Europe's Enron, Economist, Mar. 1, 2003.
49 Royal Ahold, 351 F. Supp. 2d at 344-345.
50 Sara Kehaulani Goo, Royal Ahold Writes Off $3.1 Billion On Md. Unit, Wash. Post, at E01 Oct. 3, 2003.
51 Royal Ahold, 351 F. Supp. 2d at 344-345.

vendors to falsely inflate rebate amounts.[52] In its joint venture foray, Ahold attributed the entire revenue from five joint ventures to itself when it only should have recorded revenue proportionate to its ownership of the ventures. Ahold restated its revenue for 2001 and 2002 by $24.8 billion.[53]

Parmalat

Parmalat Finanziaria SpA (Parmalat), the Italian dairy giant, has also been described as "Europe's Enron."[54] The company understated debt by $10 billion and overstated assets by $16.4 billion.[55] Parmalat's problems stemmed from a need for continual cash infusions to cover losses in certain South American ventures, to service debt, and to fund the lifestyle of CEO Calisto Tanzi and his family. To get cash from banks, the company had to look healthy. To look healthy, Parmalat either engaged in complex transactions with its 130 subsidiaries[56] or told outright lies, at one point booking a fictitious sale of $620 million worth of powdered milk to Cuba. In a typical transaction, Parmalat would send a phony invoice to a subsidiary and record an accounts receivable asset. It would then sell the subsidiary's debt to banks in exchange for cash. When the bank sought payment from the subsidiary, Parmalat lent the subsidiary cash, recording the transaction as an investment in a subsidiary rather than a loan. The bank loans Parmalat obtained meant more debt to service which required more cash infusions. [57] Parmalat issued bonds 35 times between 1995 and 2003, creating $5 billion of debt.[58] "In short, Parmalat and its confederates were operating something akin to a Ponzi scheme."[59]

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[52] Id. at 345.
[53] Id. at 345.
[54] Peter S. Goodman, From Hometown Success to Global Scandal, Wash. Post, at A01 Jan. 10, 2004.
[55] In re Parmalat Sec. Lit., 375 F. Supp. 2d 278, 282 (S.D.N.Y. 2005)[Parmalat].
[56] Peter S. Goodman, From Hometown Success to Global Scandal, Wash. Post, at A01 Jan. 10, 2004.
[57] Parmalat, 375 F. Supp. 2d at 283-284.
[58] Peter S. Goodman, From Hometown Success to Global Scandal, Wash. Post, at A01 Jan. 10, 2004.
[59] Parmalat, 375 F. Supp. 2d at 283-284.

Italian law required that Parmalat change auditors in 1999. To hide its fraud from its new auditor Deloitte & Touche, Parmalat assigned its fraudulent transactions to its Caribbean-based subsidiary Bonlat. Bonlat continued to be audited by Parmalat's old auditor, Grant Thornton.[60]

Parmalat's scheme fell under its own weight in late 2003 when it could not pay bonds, its stock lost half its value, trading was suspended for a few days, and the company announced that a Bank of America account ostensibly worth $4.9 billion did not actually exist. It filed for bankruptcy on December 24, 2003.[61]

III. Introduction to Irish and European Corporate Law

A description of basic Irish and European corporate law is included to facilitate understanding of the recent changes in Irish and European corporate law.

A. Irish Corporate Law

1. Sources of Law

Irish corporate law (called company law in local parlance) has statutory roots; corporations did not exist at either English or Irish common law. The basic statutes are contained in 11 legislative acts starting with the Companies Act 1963. Much of the current Irish regulatory scheme is relatively new, having its foundations in the Company Law Enforcement Act, 2001 (CLEA) and the Companies (Auditing and Accounting) Act 2003 (CAAA). The CLEA and the CAAA are described in detail in Part IV.

2. Form and Formation

Irish corporations come in two basic forms: private companies limited by shares (where the name of the corporation is followed with "Ltd.") and public limited companies (noted by "plc" following the company name). Forming a company requires registration with the

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[60] Id. at 284.
[61] Id. at 284.

Companies Registration Office[62] and two constitutional documents: the Memorandum of Association (Memorandum) and Articles of Association (Articles).[63] The Memorandum must contain the company name, an objects clause describing what the company has the capacity to do, a statement of limited liability, and the initial number of shares and amount of share capital.[64] The Articles are the company's bylaws. If a newly-formed company does not register Articles, model Articles found in an appendix to the Companies Act 1963 apply.[65]

3. Risk

Irish corporations have a separate legal personality and shareholder liability is limited to the amount of subscribed share capital.[66] Shares must have a par value.[67] Shareholders in a public company must pay up at least 25% of their share's nominal value whereas shares in private companies need not be paid up at all.[68] Public companies must issue a minimum of €38,092 in share capital.[69] Upon winding up, the liability of shareholders for company debts is limited to any amount unpaid on their shares.[70]

Pre-incorporation contracts entered into by subscribers are binding on the company;[71] however, companies have a limited capacity to contract (think of children today or women two centuries ago). They may only perform those acts listed in the objects clause of their Memorandum. Consequently, objects clauses often run many pages. The doctrine of *ultra vires* is still alive in Ireland, and courts may refuse to enforce contracts if they find that a company was

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[62] *See* www.cro.ie. The CRO issues certificates of incorporation.
[63] Paul Egan, Irish Corporate Procedures, 2d ed., Jordan Publishing Limited, at 19-20 (1996)[Egan].
[64] Christopher Doyle, Company Secretary, Thomson Round Hall Dublin, at 4-6 (2002)[Doyle].
[65] Egan, *supra* note 64, at 19.
[66] *See* Salomon v. A Salomon & Co Ltd (UK)(1897); PWC, Doing Business in Ireland at 13 (2004).
[67] Egan, *supra* note 64, at 21.
[68] Id. at 22.
[69] PWC, Doing Business in Ireland at 15 (2004).
[70] Doyle, *supra* note 65, at 1.
[71] Egan, *supra* note 64, at 21.

trying to do an act not listed in its objects clause.[72] However, the doctrine of *ultra vires* has been modified by statute to protect third parties who reasonably were not aware of the company's violation of its own objects clause.[73]

The courts have discretion to pierce the corporate veil if "justice…requires it."[74]

4. Return on Investment

Whether to issue dividends or to retain earnings is a board decision.[75] Dividends may only be paid out of the profits of a solvent company.[76] Companies may issue common, preferred, and redeemable shares.[77] Public companies can issue shares by offering them to the public (usually with the underwriting of a merchant bank, called "issuing house"[78]), or offering them to preexisting shareholders either as a stock dividend or under right of first refusal circumstances.[79] Public companies may list with and trade securities on the Irish Stock Exchange.[80] The stock exchange regulations are collected in the "Yellow Book."[81] Among the more important rules found in the Yellow Book are that at least a quarter of a company's shares must be in the hands of the public, a company must have been a going and solvent concern for at least three years prior to listing, and the company must have a market capitalization of at least €1.14 million.[82]

It is common in Ireland for a company with un-issued share capital to issue "bonus shares." Bonus shares are a dividend to existing shareholders of shares representing the value of

[72] *See* Companies (Amendment) Act 1983 §45.
[73] *See* Companies Act 1963 § 8.
[74] Power Supermarket v. Crumlin Investments and Dunnes Stores (Crumlin) Ltd (1981)(lifting the corporate veil on a group structure because "the justice of the case so requires it"). *See also* The State (McInerney & Co Ltd) v. Dublin County Council (1985)("The arm which lifts the corporate veil must be that of equity").
[75] Bond v. Barrow Hematite Steel Co (1902).
[76] Eavan Murphy, Irish Company Law Revision, Gill & MacMillan, at 41 (1999)[Murphy]. *See also* Part IV of Companies Act 1983.
[77] Egan, *supra* note 64, at 32.
[78] Doyle, *supra* note 65, at 26.
[79] Murphy, *supra* note 77, at 26.
[80] Egan, *supra* note 64, at 34.
[81] Doyle, *supra* note 65, at 27.
[82] Id. at 28.

the capital account. They are not simple share dividends (i.e., a 3 for 1 split where the holder of a share worth $100 receives three shares each worth $33.33). They are a distribution of rights to existing capital (i.e., a 1 for 3 bonus will give a shareholder owning three shares worth $100/share one share that is also worth $100. The value of his shareholdings increases from $300 to $400). The company's capital is not diminished. Instead, the rights to that capital are divided amongst the current shareholders.[83]

Companies may issue bonds (commonly called debentures). Irish companies usually secure their debentures with company assets – as such, they are closer to mortgages than American-style debt offerings.[84] A debenture-holder can secure his debt via either a fixed charge or a floating charge. A fixed charge ties the security to a specific asset, whereas a floating charge becomes a fixed charge ("crystallizes") only if the company goes bankrupt or the parties agree to a specific time or event.[85] Fixed charges have priority over floating charges and both have priority over shareholder interests.[86]

5. Corporate Control

Shareholders

Shareholders are often called members. Public companies must have a minimum of two members.[87] Private companies may have a minimum of one member and a maximum of 50 members (excluding current and former employees).[88] Members must meet at least once in a calendar year and meetings cannot be more than fifteen months apart.[89]

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83 Id. at 244.
84 Id. at 193.
85 Murphy, *supra* note 77, at 47-49.
86 Id. at 49.
87 Egan, *supra* note 64, at 31.
88 Id. at 31.
89 Id. at 33.

Shares in public companies are freely transferable whereas shares in private companies may be transferred only with board approval.[90]

Directors and Secretaries

All companies must have at least two directors and one company secretary.[91] The secretary may be one of the two directors. The secretary need not be a natural person - often an accounting firm acts as secretary for several companies.[92] The directors and secretary are collectively the officers of the company.[93]

Directors have almost unlimited powers to exercise the objects of the company.[94] This power is limited by the fiduciary nature of the position and may be further mitigated by the Articles of Association and shareholder resolutions.[95] If a director's failure to properly oversee the company leads to insolvency, the director may be personally liable for the debts of the company.[96]

The secretary is often the chief administrative officer and thus has the agency power to contract for the company.[97] The secretary's functions are wide-ranging but ill-defined; he is to oversee the administration of the company and compliance with the Companies Acts. Perhaps his most important duty is to make and file the annual return to the Registrar of Companies.[98]

Irish law has no mandatory requirements for board meetings.[99]

Each year, a third of the directors must offer to resign.[100]

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[90] Murphy, *supra* note 77, at 33.
[91] Companies Act 1963 §§ 174-175
[92] Doyle, *supra* note 65, at 58.
[93] Companies Act 1963 § 2
[94] Doyle, *supra* note 65, at 46-47.
[95] Id. at 46.
[96] Companies Act 1990 § 204
[97] Murphy, *supra* note 77, at 67.
[98] Doyle, *supra* note 65, at 230.
[99] Egan, *supra* note 64, at 22.
[100] Murphy, *supra* note 77, at 58.

Examiners

A court may appoint an examiner when a company is unlikely to be able to pay its debts. Appointment of an examiner is a step to save a company before a receiver or liquidator is appointed.[101] The goal of the examiner is to give a distressed company "breathing space," akin to the protection provided by Chapter 11 of the U.S. Bankruptcy Act 1978.[102] The examiner researches the affairs of the company and reports to the court whether he thinks the company can continue as a going concern and what changes must be made to foment that goal. The court may order that the examiner take over management from the board.[103]

Receiver

Debenture-holders whose debt has fallen into arrears can ask a court to appoint a receiver. The receiver's task is to sell the attached assets and pay off the debenture.[104] The appointment of a receiver suspends directors' powers with regard to the charged asset.[105] The receiver is a fiduciary to the debenture holder. His duty to the company is to report a "statement of affairs."[106] The appointment of a receiver is often a last step before bankruptcy.[107]

Liquidator

When a company is bankrupt and folds, a court appoints a liquidator.[108] In the case of voluntary liquidations, the company appoints its own liquidator.[109] In either case, the liquidator is a fiduciary to the company who must sell the assets, pay the debts, and distribute surplus.[110]

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[101] Id. at 91.
[102] *See* Doyle, *supra* note 65, at 259.
[103] Murphy, *supra* note 77, at 92.
[104] Id. at 54.
[105] Id.
[106] Id. at 56.
[107] Doyle, *supra* note 65, at 199.
[108] Companies Act 1963 § 225
[109] Id. § 258
[110] Murphy, *supra* note 77, at 97.

6. Duration

Once a company is formed it has perpetual succession. The company ceases to exist when it is wound up by its members (voluntary liquidation) or when a court orders a bankrupt company to fold (compulsory liquidation).[111] Creditors may seek voluntary liquidation, a sort of private bankruptcy where the company deliberately agrees to fold and pay off debts.[112]

B. European Corporate Law

Current E.U. company law is comprised of three Regulations,[113] thirteen Directives or Proposals for Directives,[114] and three Recommendations.[115] While corporations must still

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[111] Id. at 6. *See also* Companies Act 1963 § 213 for the rules on court-ordered windups.
[112] Murphy, *supra* note 77, at 97.
[113] Council Regulation (EEC) 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG); Council Regulation (2001/2157/EC) of 8 October 2001 on the Statute for a European Company SE *supplemented by* Council Directive (2001/86/EC) of 8 October 2001 supplementing the Statute for a European Company with regard to the involvement of employees; Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

[114] First Council Directive 68/151/EEC of 9 Mar. 1968 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community (OJ L 065, 14/03/1968, p. 8); Second Council Directive 77/91/EEC of 13 Dec. 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent (OJ L 026, 31/01/1977, S. 1); Third Council Directive 78/855/EEC of 9 Oct. 1978 based on article 54(3)(g) of the Treaty concerning mergers of public limited liability companies (OJ L 295, 20/10/1978, p. 1); Fourth Council Directive 78/660/EEC of 25 July 1978 based on article 54(3)(g) of the Treaty on the annual accounts of certain types of companies (OJ L 222, 14/08/1978, p. 11); Amended proposal for a Fifth Directive founded on article 54(3)(G) of the Treaty concerning the structure of public limited companies and the powers and obligations of their organs (OJ C 240, 09/09/1983, p.2); Sixth Council Directive 82/891/EEC of 17 Dec. 1982 based on article 54(3)(g) of the Treaty, concerning the division of public limited liability companies (OJ L 378, 31/12/1982, p. 47); Seventh Council Directive 83/349/EEC of 13 June 1983 based on the article 54(3)(g) of the Treaty on consolidated accounts (OJ L 193, 18/07/1983, p. 1); Eighth Council Directive 84/253/EEC of 10 Apr. 1984 based on article 54(3)(g) of the Treaty on the approval of persons responsible for carrying out the statutory audits of accounting documents (OJ L 126, 12/05/1984, p. 20); Proposal for a Tenth Directive of the Council based on article 54(3)(g) of the Treaty concerning cross-border mergers of public limited companies (OJ C 023, 25/01/1985, p. 11); Eleventh Council Directive 89/666/EEC of 21 Dec. 1989 concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State (OJ L 395, 30/12/1989, p. 36); Twelfth Council Company Law Directive 89/667/EEC of 21 Dec. 1989 on single-member private limited-liability companies (OJ L 395, 30/12/1989, p. 40); Proposal for a Thirteenth European Parliament and Council Directive on company law concerning takeover bids (OJ C 162, 06/06/1996, p. 5); Proposal for a Fourteenth Directive on Liquidation (unofficially published in Lutter, Europaisches Unternehmensrecht 302 ff.
[115] Commission Recommendation (2001/256/EC) of 15 November 2000 on quality assurance for the statutory audit in the European Union: minimum requirements; Commission Recommendation (2001/453/EC) of 30 May 2001 on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of

incorporate in Member States, the E.U. has taken steps towards the European Company and two of these Regulations deal with company form. In 1985, the European Economic Interest Grouping (EEIG) became the first supranational company form in Europe.[116] The EEIG allowed a framework for independent companies to cooperate but it "gained only limited importance."[117] In 2001, the E.U. passed a Regulation creating the European Company (Societas Europaea or SE).[118] An SE is able to operate throughout Europe on the basis of one uniform legal and administrative regulation. Creating an SE is rather difficult as the company must have a minimum share capital of €120,000 and cannot be formed directly but must emerge from a pre-existing Member State-incorporated company.[119]

One other E.U. Regulation affecting corporations deals with accounting standards. The statute mandates that publicly traded companies meet International Accounting Standards Board (IASB) standards when preparing public accounts.[120]

E.U. company law Directives mandate corporate disclosure requirements, including disclosure of a company's constitutional documents; minimum capital requirements for public companies; that Member States make laws governing mergers and divisions; the layout and content of balance sheets and profit & loss statements; that companies with subsidiaries prepare consolidated accounts; qualifications for auditors; rules for branches of companies operating in other Member States; and the existence of single member private limited liability companies.[121]

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companies; Commission Recommendation (2002/590/EC) of 16 May 2002 on "Statutory Auditors' Independence in the EU : A Set of Fundamental Principles."

[116] *See* Council Regulation (EEC) 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG).

[117] Andreas Kellerhals & Dirk Truten, Creation of the European Company, 17 Tul. Eur. & Civ. L.F. 71, 75 (2002).

[118] *See* Council Regulation (2001/2157/EC) of 8 October 2001 on the Statute for a European Company SE *supplemented by* Council Directive (2001/86/EC) of 8 October 2001 supplementing the Statute for a European Company with regard to the involvement of employees.

[119] Kellerhals, *supra* note 119, at 72, 77-78.

[120] Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

[121] *See supra* n.113.

E.U. Commission company law Recommendations call for quality assurance systems for statutory audits; recognition, measurement, and disclosure of environmental issues; and propose fundamental principles for statutory auditors.[122]

IV. Government Response to Scandal

A. U.S. Response: SOX

The Sarbanes-Oxley Act of 2002 became law on July 30, 2002.[123] It changes the oversight and responsibilities numerous corporate actors.

1. Auditor Regulation

Prior to SOX, the auditing profession was self regulated.[124] That changed with the establishment of the Public Company Accounting Oversight Board (PCAOB).[125] The PCAOB is a nonprofit corporation[126] that regulates auditors by setting audit standards and investigating violations of SEC rules and regulations. It can sanction violators with fines of up to $15 million, censures, removal from auditing projects, limitations on activities, and suspension.[127] Its activities are funded by mandatory fees paid by the companies it regulates.[128] Accounting firms must register with the PCAOB before issuing audit reports to the public.[129]

In the realm of document retention, audit firms must maintain work papers for seven years[130] or longer if the PCAOB chooses.[131]

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122 *See supra* n.114.
123 Hamilton, *supra* note 4, at 6.
124 Jonathan Shirley, International Law and the Ramifications of the Sarbanes-Oxley Act of 2002, 27 BC Int'l & Comp. L. Rev. 501, 506 (2004).
125 SOX § 101.
126 15 U.S.C. § 7211(a)-(b)(2005).
127 SOX § 105; 15 U.S.C. § 7215(2005).
128 SOX § 109; 15 U.S.C. § 7219(2005).
129 SOX § 102; 15 U.S.C. § 7212(2005).
130 SOX § 103; 15 U.S.C. § 7213(2005).
131 SOX § 104(e); 15 U.S.C. § 7214(2005).

Large accounting firms (those that audit at least 100 clients) can expect an annual PCAOB inspection, and smaller firms can expect a government audit at least every three years.[132]

Auditing firms may not provide non-audit services to the public companies they audit. "The banned services include financial information system design and implementation, appraisal or valuation services, internal auditing services, investment banking services, legal and expert services unrelated to the audit, brokerage services, and actuarial services."[133] The audit partner having primary responsibility for a client's audit must be rotated every 5 years.[134]

SOX applies to foreign accounting firms just as it applies to American firms.[135]

2. Board Regulation

Congress legislated board composition by mandating that public companies have an audit committee which is solely responsible for choosing, paying, and receiving the work of external auditors.[136] Congress also mandated that directors who sit on the audit committee have no consulting, advisory, or compensatory connection to the corporation or its subsidiaries.[137] The audit committee must establish procedures to receive complaints about accounting matters and receive confidential, anonymous submissions by employees of concerns regarding accounting practices.[138] An auditor's client is now the audit committee, not senior management.[139]

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[132] SOX § 104; 15 U.S.C. § 7214(2005).
[133] Romano, *supra* note 4, at 1533. *See also* SOX § 201.
[134] SOX § 203.
[135] Id. § 106; 15 U.S.C. § 7216(2005).
[136] SOX § 301.
[137] Id.
[138] Id.
[139] Lucci, *supra* note 4, at 225.

3. Executive Regulation

SOX prevents corporations from making loans to executives or directors.[140] Executives at Enron, WorldCom, Tyco International, and Adelphia Communications were given hundreds of millions in loans.[141]

A company's CEO and CFO must sign financial statements to certify that the statements do not contain material misstatements or omissions and "fairly present" their firm's financial condition.[142] The signing officers certify that they are responsible for establishing and maintaining internal controls.[143] SOX provides criminal penalties for violating the certification requirement.[144] Implicit in this certification requirement is that executives implement internal controls and that the executives monitor these controls;[145] SOX makes that requirement explicit by requiring corporations to file reports assessing the internal controls.[146]

If executive misconduct causes a corporation to restate its financial reports, the malfeasant executives must forfeit bonuses, incentive-based compensation, and any profit from the sale of stock or options made during the previous year.[147]

4. Attorney Regulation

Like auditors, attorneys were primarily self-regulated. Congress created a "report up, report out" system where lawyers who find evidence of financial misconduct must report their findings to the corporation's CEO or chief in-house counsel.[148] If the executive does not remedy the situation, the attorney must report his findings to the audit committee or the board of

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[140] SOX § 402(a). SOX exempts loans made in the "ordinary course of the consumer credit business" or loans which are "generally made available…to the public." SOX § 402(a).
[141] Romano, *supra* note 4, at 1538.
[142] SOX § 302.
[143] Id. § 302(a)(4); 15 U.S.C. § 7241(2005).
[144] SOX § 906(a).
[145] Romano, *supra* note 4, at 1540.
[146] SOX § 404.
[147] Id. § 304; 15 U.S.C. § 7243(2005)
[148] SOX § 307; 15 U.S.C. § 7245(2005).

directors.[149] If the situation is still not remedied, the attorney should make a "noisy withdrawal" where he publicly quits his engagement with the company.[150]

Congress also granted the Securities and Exchange Commission (SEC) power to create standards of professional conduct for attorneys appearing before it.[151]

B. Irish Response

1. Pre-2001 Governance Provision: Section 150 Orders

Under Section 150 of the 1990 Companies Act, a court can bar misbehaving directors from directing *any* company for five years.[152] Section 160 is even harsher on persons convicted of crimes in relation to companies: they are automatically barred from acting as director, secretary, auditor, receiver, liquidator, or examiner.[153]

2. CLEA

In the 1990s, Irish corporations had a dismal record when it came to filing corporate compliance returns. In 1997, for example, only 13% of the 136,000 companies that had to file returns with the Registrar of Companies actually did so.[154] The CLEA responded to this problem (among others) by establishing a corporate "watchdog" and by providing for harsher criminal penalties for officers of companies that failed to file their company's return.[155]

Director of Corporate Enforcement

The CLEA creates the Director of Corporate Enforcement (DCE or Director), a regulator with broad powers over Irish companies.[156] The Director has the power to investigate and

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[149] SOX § 307; 15 U.S.C. § 7245(2005).
[150] Lucci, *supra* note 4, at 222.
[151] 15 U.S.C. § 7245(2005).
[152] Companies Act 1990 § 150. Commonly known as a "Section 150 Order."
[153] Companies Act 1990 § 160.
[154] Brian Walker, Company Directors: All is About to Change! The New Company Law Enforcement Act of 2001, 8 Comm. L. Pract. 151, 151 (2001).
[155] Company Law Enforcement Act (2001) § 59 [CLEA].
[156] Id. § 7.

prosecute breaches of the Companies Acts,[157] supervise the activity of liquidators and receivers,[158] demand to see a company's minutes without giving a reason to see them,[159] and demand to see any other books or documents if he suspects fraud.[160] The DCE is to be made privy to the appointment of a receiver and may oversee his work.[161] The Director can petition a court for search warrants and he has the police power to search a dwelling for material information.[162] Failing to comply with a DCE document request, submitting false or misleading documents to the DCE, or destroying documents are criminal offenses.[163] The Director can petition the court to disqualify a director from involvement in the management of a company, and, if the court approves the petition by issuing a "Section 150 Order," the director is disqualified for five years.[164]

Board Regulation

The major duty that the CLEA imposes on directors and secretaries is the obligation to "ensure that the requirements of the Companies Acts are complied with by the company."[165] Prior to the CLEA, officers merely had to not break the law; now they must actively comply with its direction, or face criminal liability for failure to do so.

As far as individuals are concerned, a bankrupt person may not be a director.[166] The DCE can require a director he reasonably believes to be bankrupt to make a statement of his personal financial position. The court has the power to freeze the assets of an officer if the court thinks

[157] Id. § 12(a),(c).
[158] Id. § 12(e).
[159] Id. § 19.
[160] Id. § 29.
[161] Id. §§ 52-53.
[162] Id. § 30.
[163] Id. § 29.
[164] Id. § 40. *See also* Companies Act 1990 § 150.
[165] CLEA § 100.
[166] Companies Act 1963 § 176.

that the officer might frustrate a civil judgment by disposing of his own or company assets.[167] Application for such an order may be made by Companies, directors, shareholders, creditors, receivers, liquidators, or the DCE.[168]

Auditor Regulation

The DCE can "demand" to see the qualifications of an auditor and failure to produce them is a criminal offense.[169] Accounting bodies must report evidence of a members' breach of the Companies Acts.[170]

Similar to SOX's "report up, report out" provision,[171] Irish auditors who reasonably believe that a company or director has broken the Companies Acts must report that belief to the DCE.[172]

Bankruptcy and Windups

Prior to the CLEA, Irish courts had the power to examine directors' conduct only during involuntary wind-ups.[173] Now, courts and the DCE can supervise even voluntary wind-ups.[174] The court may order inspection of a company's books and may order a director to make a statement to the court concerning any company property he may have in his possession or any debts he owes to the company.[175] The director may not refuse to answer for fear of incriminating himself.[176]

The liquidator of a bankrupt company must apply for Section 150 Orders for the removal of all of the company's directors, regardless of who was actually responsible for the

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[167] CLEA § 55.
[168] Id.
[169] CLEA § 72.
[170] Id. § 73.
[171] *See* SOX § 307, 15 U.S.C. § 7245(2005).
[172] CLEA § 74.
[173] Companies Act 1963 § 245.
[174] Id. § 49.
[175] Id. *See also* id. at § 43.
[176] Id. §§ 44 & 49.

bankruptcy.[177] If a liquidator uncovers a criminal offense during the course of his work, he must report it both to the state criminal prosecutor and the DCE.[178] The Director can demand to see liquidators' work regardless of the solvency of the winding-up company.[179] The DCE has oversight of liquidators and of their professional bodies.[180]

3. CAAA

Auditor Regulation

The CAAA established the Irish Auditing and Accounting Supervisory Authority (IAASA or Authority).[181] The objects of the IAASA are to supervise how accounting bodies monitor and regulate their members, to promote adherence to professional standards in the accounting industry, to monitor whether companies' accountings comply with the Companies Acts, and to be a source of advice to the Minister for Enterprise, Trade and Employment.[182] To carry out its objects, the Authority has the power to recognize accounting bodies;[183] approve accounting bodies' investigatory procedures, constitutions, and bylaws;[184] oversee any investigations that accounting bodies may undertake and sanction those bodies that do not comply with approved investigatory procedures;[185] investigate and sanction breaches of accounting standards;[186] and review companies' annual accounts.[187] The Authority has the power to review a company's accounting if it questions whether that accounting complies with the

[177] Id. § 56.
[178] Id. § 51. In Ireland, criminal prosecutions are handled by the Director of Public Prosecutions (DPP).
[179] Id. § 57.
[180] Id. § 56-57.
[181] Companies (Auditing & Accounting) Act (2003) § 5(1)[CAAA].
[182] Id. § 8(1).
[183] Id. § 9(2)(a).
[184] Id. § 9(2)(c).
[185] Id. §§ 9(2)(d)-(e), 23.
[186] Id. §§9(2)(f), 24.
[187] Id. §§9(2)(l), 26.

Companies Acts.[188] If the Authority finds accounting irregularities, it can petition the court to force the company to revise its accounts.[189]

The CAAA does not bar auditors from doing non-audit work; it only requires that companies disclose what they paid their auditor for both audit and non-audit work.[190]

Compliance Statements

Companies must include in their annual accounting a statement as to whether their accounts have been prepared in accordance with "applicable accounting standards." If their accounting does not comply with those standards, the company must include a statement describing material departures, the effects of any departures, and the reasons for such a departure.[191] Failure to include such a statement is a criminal offense.[192] Companies must disclose the accounting policies they followed in determining the numbers on their balance sheets and profit & loss statements.[193]

Directors must prepare statements that describe their company's internal financial procedures for securing compliance with the Companies Acts, Irish tax law, and "any other enactments that provide a legal framework within which the company operates and that may materially affect the company's financial statements."[194] Directors must then acknowledge that they are responsible for securing compliance and whether they are of the opinion that "they used all reasonable endevours to secure the company's compliance with its relevant obligations."[195]

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[188] Id. § 26.
[189] Id. § 26(6).
[190] Id. § 44.
[191] Id. § 41. This provision is often referred as the "Comply or Explain" requirement. It contrasts with what is commonly known as the "Comply or Else" provision found in SOX § 302.
[192] CAAA § 41.
[193] Id. § 43.
[194] Id. § 45.
[195] Id.

Auditors must then review the directors' statements and decide if they are "fair and reasonable."[196]

Audit Committees

Section 42 of the CAAA requires that public companies establish audit committees. The audit committee must review the company's accounts for compliance with applicable accounting standards, monitor the performance and quality of the auditor's work and independence from the company, and report to the board of directors its choice of auditor and its recommendation on awarding non-audit work to auditors (though the ultimate choice of auditor still lies with the board as a whole).[197] The audit committee must have at least two members, and members may not currently or within the last three years have been employees of the company.[198]

C. E.U. Response

1. Action Plan

On May 21, 2003, the European Commission (Commission) issued a report entitled "Modernising Company Law and Enhancing Corporate Governance in the European Union" (Action Plan).[199] The Action Plan contains proposals for legislative and non-legislative action that the E.U. plans to implement over the coming years. While the Action Plan covers many subjects,[200] this paper only reviews those germane to corporate governance. The Commission concluded that there was no need for an E.U.-wide, super-national corporate governance code.[201] It instead proposed that the E.U.'s role in improving corporate governance was to facilitate

[196] Id.
[197] Id. § 42.
[198] Id.

[199] Communication from the Commission to the Council and the European Parliament -- Modernising Company Law and Enhancing Corporate Governance in the European Union -- A Plan to Move Forward, COM (2003) 284 final (May 2003)[Action Plan].
[200] The Action Plan addresses corporate governance, capital maintenance and alteration, groups & pyramids, corporate restructuring and mobility, the European private company, the European Co-operative Society and other E.U. legal forms of enterprise, and enhancing the transparency of national legal forms of enterprise.
[201] Action Plan at 11.

convergence and exchange of best practices.[202] The Action Plan addressed ways to enhance corporate governance disclosure, strengthen shareholders' rights, modernize the board of directors, and coordinate Member State corporate governance efforts.

Enhancing Corporate Governance Disclosure

The Action Plan proposed that public companies include a statement of their corporate governance structure in their annual reports. The statement should include a list of shareholders' rights and how to exercise them, a description of how the board and its committees operate, a list of major shareholders and how their ownership affects voting and control rights, disclosure of any other relationships between the company and these major shareholders, disclosure of material transactions with other related parties, and disclosure of the existence and nature of a risk management system.[203] The Commission proposed that a Directive would best foment these goals.[204]

The Action Plan further proposed that institutional investors disclose their investment policy and their policy on exercising voting rights, and to disclose, when beneficiaries ask, how these voting rights have been exercised in a particular case.[205]

Strengthening Shareholders' Rights

The Commission proposed that companies use electronic facilities to send relevant information to shareholders in advance of shareholder meetings.[206] This would allow shareholders to more effectively exercise their rights to ask questions, to table resolutions, and to participate and vote in abstentia by electronic means.[207] The Commission suggested that a

[202] Id. at 11-12.
[203] Id. at 12-13.
[204] Id. at 13.
[205] Id.
[206] Id.
[207] Id. at 14.

Directive would best solve the "legal difficulties" involved in implementing this part of the plan.[208]

Modernizing the Board of Directors

The Action Plan suggests that independent directors should make decisions where executive directors have conflicts of interest. The proposed areas include director remuneration and supervision of the audit.[209] The Action Plan proposes that shareholders receive information regarding individual director's remuneration and that shareholders approve any director share or option compensation.[210] Directors should be collectively responsible for financial statements and the annual corporate governance statement. To force that responsibility on directors, the Commission proposed that shareholders who hold a certain percentage of shares have a special investigation right into the affairs of the company, that directors be personally liable for failing to adequately deal with the company's debts, and that directors be disqualified across the E.U. for issuing misleading company statements.[211] The Commission proposed that the E.U. adopt a Recommendation to effect these changes.[212]

Coordinating Member State Corporate Governance Efforts

The Commission suggested a "European Corporate Governance Forum" (Forum) to serve as a clearinghouse for coordination and convergence of Member State governance laws.[213] The Forum came into existence on October 18, 2004.[214]

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[208] Id.
[209] Id. at 15.
[210] Id. at 16.
[211] Id.
[212] Id.
[213] Id. at 17.
[214] *See* the Commission's announcement on October 18, 2004, *available at* http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/04/1241&format=HTML&aged=0&language=EN&guiLanguage=en (last visited November 12, 2005).

2. Transparency Directive

On December 15, 2004, the E.U. adopted a Directive on minimum transparency requirements for listed companies.[215] The goal of the Directive is to improve the information available to investors, thus helping them allocate funds on the basis of a more informed assessment of a company. The Directive seeks to ensure that investors receive interim management statements from companies who do not publish quarterly reports, and bi-annual financial reports from issuers of new bonds. In addition, all securities issuers will have to provide annual financial reports within four months of the end of the financial year. The Directive is due to be implemented no later than January 2007.

3. Recommendations on Director's Remuneration and the Role of Independent Directors

On October 6, 2004, the Commission adopted Recommendations on directors' remuneration[216] and on the role of independent non-executive directors on listed companies' boards.[217] The former recommends that Member States force listed companies to disclose their policy on directors' remuneration and tell shareholders how much individual directors are earning and in what form, and ensure shareholders are given adequate control over these matters and over share-based remuneration schemes. The latter focuses on the role of non-executive or supervisory directors in key areas where executive or managing directors may have conflicts of interest. It recommends minimum standards for the qualifications, commitment, and independence of non-executive or supervisory directors.

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[215] Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC.

[216] Commission Recommendation (2004/913/EC) of 14 December 2004 on fostering an appropriate regime for the remuneration of directors of listed companies.

[217] Commission Recommendation (2005/162/EC) of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board.

4. Accounting Directives

On May 31, 2001, the E.U. adopted a Directive mandating that Member States permit or require the use of fair value valuation methods to account for certain classes of financial instruments in companies' annual financial statements.[218] This Directive will therefore enable European companies to prepare annual financial statements in accordance with international developments. Companies will be required to provide additional information in the notes to the accounts on the items that have been valued at fair value.

On June 18, 2003, the E.U. adopted a Directive to bring existing E.U. rules into line with current best practice.[219] It requires all E.U. companies listed on a regulated market to use International Accounting Standards from 2005 onwards and allows Member States to extend this requirement to all companies.

5. Proposal for an Auditing Directive

The E.U. responded to scandals in the U.S. and Europe with a March 2004 proposal for a directive that would tighten audit rules in E.U. Member States.[220] Inspired by SOX's establishment of the PCAOB, [221] the proposal calls for public oversight of auditors and regulatory cooperation with the other states' oversight bodies.

The proposed directive would end European auditors' self regulation by mandating that Member States set up regulatory bodies like the PCAOB and the IAASA. Public companies

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[218] Directive 2001/65/EC of the European Parliament and of the Council of 27 September 2001 amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC as regards the valuation rules for the annual and consolidated accounts of certain types of companies as well as of banks and other financial institutions.
[219] Directive 2003/51/EC of the European Parliament and of the Council of 18 June 2003 amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings.
[220] Commission Proposal of 16 March 2004 for a Directive of the European Parliament and of the Council on statutory audit of annual accounts and consolidated accounts and amending Council Directives 78/660/EEC and 83/349/EEC.
[221] *But see* Commission Proposal of 16 March 2004 for a Directive of the European Parliament and of the Council on statutory audit of annual accounts and consolidated accounts and amending Council Directives 78/660/EEC and 83/349/EEC p.2 ("This proposal is not a knee-jerk reaction to recent corporate scandals. It is the logical consequence of a reorientation of the EU policy on statutory audit started back in 1996.").

would be required to establish American-style independent audit committees responsible for hiring, overseeing, and firing auditors. Auditors from outside the E.U. would have to register with the Member State's auditor regulator. The proposal does not call for a complete ban on auditors providing non-audit services; it instead would ban the provision of these services if doing so would compromise independence and in all cases would ban auditor involvement in making company management decisions.

V. Analysis: Proportionality and Convergence

At least two issues come up when discussing international corporate scandals and government responses: whether the responses are proportionate to the problem and whether governments are coming up with similar solutions to similar problems.

A. Proportionality

Commentators often note how quickly SOX became law. Enron collapsed on November 9, 2001, and President George W. Bush signed SOX into law less than nine months later.[222] By contrast, the Irish and the Europeans took more time before passing legislation. The reason for this disparity in time may be founded on the size of the problems.

1. American Response

America had a much bigger problem than the Irish or the Europeans. American scandals were measured in billions, Irish only in millions. Furthermore, an American imprimatur touches every old-world scandal: Elan is headquartered in New York, trades on the NYSE, and conducts its activities mainly in the U.S. AIB's troubles came from an American trader working at an American subsidiary. It was sued by an American investor in an American court. Ahold's

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[222] Hamilton, *supra* note 4, at 6.

problems were the result of misfeasance at an American subsidiary.[223] Parmalat could not have hid so much debt for so long without the complicity of Bank of America and American auditors Grant Thornton and Deloitte & Touche. Scandals in Ireland and Europe are American scandals too.

2. Irish Response

When Ireland passed the CAAA, it responded with more harshness to less of a problem. The CAAA contains many provisions similar to SOX: both created auditing regulatory bodies; both address auditors and non-audit work; both mandate audit committees; both have "report up, report out" provisions; and both require companies and directors to certify the accuracy of financial statements. However, there are numerous differences within the similarities: the CAAA has more criminal penalties for the IAASA, DCE, and DPP to enforce; American auditors may not provide non-audit services whereas Irish auditors are only barred from providing services that lead to conflicts of interest; Irish directors, even if they are not currently employed by the company, may not sit on the audit committee if they were employed within the last three years; SOX allows attorneys to "report up, report out" whereas CLEA requires auditors to report company law breaches to the DCE; Ireland requires directors, companies, and auditors to sign off on the accuracy of financial statements whereas the U.S. only requires directors and companies to sign compliance statements.[224] Furthermore, Irish companies have to deal with the DCE whose sole job is to enforce the Companies Acts—their criminal provisions and all. While certain provisions of SOX may be harsher than certain provisions of CAAA, when one considers

[223] *But see* Europe's Enron, Economist, Mar. 1, 2003 (The fact that Ahold's accounting problems occurred primarily at an American subsidiary "has led some observers to say that this is less a European problem than yet another American accounting failure. Such an outlandish claim absolves Ahold's bosses of responsibility for their acquisitions and ignores the persistent, firm-wide tendency to test the limits of acceptable accounting.").
[224] *See e.g.* PJ Henehan, Section 45 will kill Irish competitiveness, Irish Times, Feb. 25, 2005 ("While there is a cost of scandal, there is also a cost of compliance. In this regard, Section 45 goes beyond what is required of companies in other jurisdictions, particularly the US.").

the full extent of the Companies Acts (i.e., Section 150 Orders), the power of the DCE, and the fact that Ireland had less of a corporate crisis to begin with, Ireland's attempts to prevent future corporate malfeasance are disproportionate to the problem.

Surely Ireland had corporate problems, but they were compliance issues, not governance issues. Ireland responded to its compliance problems: it passed the CLEA which created the DCE to act as a watchdog. The CLEA deals more with compliance than governance – it was passed in early 2001, before Enron and other problems came to light in late 2001. It forces companies to answer to the government, not to stakeholders. Even so, the CLEA is harsh: the DCE has incredible power – police power, prosecutorial power, regulatory power, banishment power. The Director himself can make a company's life very hard; there is not really any one American regulator with that much power.

3. E.U. Response

This quote aptly demonstrates the need for E.U. corporate regulation:

> Italy has a reputation for poor corporate governance combined with the shameless exploitation of minority shareholders. But much the same can be said of other European countries, including France, the Netherlands and Switzerland, where this week Adecco, the world's largest temporary-employment agency, said it expects to delay the announcement of its 2003 results because of "possible accounting, control and compliance issues...in certain countries". Most European countries have mere codes of practice for corporate governance, rather than legal statutes, and progress towards meeting the standards of the codes has been patchy at best.[225]

The E.U. has taken an almost academic response to scandals, publishing studies and proposals rather than much binding legislation. The main conclusion of the Action Plan was that the E.U. did not need a Union-wide corporate governance code.[226] The E.U. sees its role as a

[225] Parma splat - Europe's corporate governance, Economist, Jan. 20, 2004. NB: Switzerland is not a member of the E.U.
[226] Action Plan at 11.

body that facilitates exchange of best practices rather than a creator or mandator of practices.[227] As such, it will be for the E.U. to study the effects of SOX, CLEA, and CAAA and propose their pearls to other European countries. It created the European Corporate Governance Forum to do just that.

The E.U. legislation passed this millennium has mandated certain practices, but the E.U. legislated only to foment its convergence goal. Convergence is taken up at length in Part V.B.

B. Convergence

Ideas come from the Americans, get distilled by the Europeans, and applied by states as they see fit. Ireland saw fit to copy the audit regulator, audit committee, and have directors personally sign off on financial statements. European states do not wholly plagiarize American statutes, however. To use Ireland as an example, their audit regulator, audit committees, and sign-off rules, though inspired by the Americans, have a local flare. Nonetheless, corporate governance rules are converging and Irish and European laws passed since the turn of the millennium show this movement.

1. World-Wide Catalyst: Enron

Enron was a catalyst around the world. The antecedent of the E.U. Action Plan was a desire to "review further corporate governance and auditing issues in the light of the Enron case."[228] The Economist wrote that "Europeans should stop smugly believing that corporate malfeasance is an American vice that cannot occur in the old continent. Instead, they should fix their corporate-governance and accounting problems with as much vigour as their American

[227] Id. at 11-12.
[228] See Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe (November 4, 2002), available at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf (last accessed November 12, 2005).

cousins showed after the Enron wake-up call."[229] SOX "seems to have kicked Europe's protracted process into gear. 'Parmalat was an extra boost, but the real motor was Sarbanes-Oxley,' says Neil Lerner, head of regulatory issues at KPMG, an auditing firm. 'Europe had to stand up and be counted.'"[230]

European scandals sparked European action too. "The [Ahold] scandal should dispel claims about the supposed inherent superiority of continental Europe's two-tier boards over Anglo-Saxon unitary boards. Ahold's supervisory board was at least as dominated by [Ahold CEO Cees] van der Hoeven as any American board was by its chief executive."[231]

2. Convergence in Regulation

As night follows day, the IAASA followed the PCAOB in taking away auditor self-regulation. If the E.U. had its way, auditors' self-regulation would end because every Member State would set up an auditor regulatory body of its own.[232] The PCAOB and IAASA surely have their differences: the members of the PCAOB are all independent, whereas the IAASA membership is comprised of accounting and other financial bodies.[233] But to the average auditor, he is now governed by and paying fees to a government body that did not exist prior to the corporate scandals.

All three governments would require foreign auditors to register with a regulatory body, and all three seek to tighten rules about how auditors provide non-audit work.

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[229] Europe's Enron, Economist, Mar. 1, 2003.
[230] More rules, Economist, March 20, 2004. A more pessimistic view holds that American corporate scandal "provided an occasion for 'political activism' juicy enough for any well-taught politician and bureaucrat willing to extract rents." Enriques, *supra* note 4, at 916.
[231] Europe's Enron, Economist, Mar. 1, 2003.
[232] Commission Proposal of 16 March 2004 for a Directive of the European Parliament and of the Council on statutory audit of annual accounts and consolidated accounts and amending Council Directives 78/660/EEC and 83/349/EEC.
[233] CAAA § 6. The following bodies are statutory members of the Authority: Irish Business and Employees Confederation, Irish Congress of Trade Unions, Irish Association of Investment Managers, Irish Stock Exchange, Pensions Board, Irish Financial Services Regulatory Authority, Revenue Commissioners, Director of Corporate Enforcement, and the Law Society of Ireland. CAAA (6)(2).

3. Convergence in Board Structures

Audit committees are "a new concept in Irish company law."[234] Now, the U.S. and Ireland require them and the E.U. wants to mandate them. All three governments insist that the committees be comprised of independent directors even though they define independence differently. Here as elsewhere there are issues of efficacy: "[t]he parallels with America's corporate scandals do not end with the fallibility of auditors. The lack of independence of non-executive directors on the board is another issue in common. Parmalat's was stuffed with family members and local cronies. Despite a 1999 reform that imposed independent directors on listed Italian companies, big ones such as Parmalat were allowed to opt out."[235]

4. Convergence in Transparency

Irish and American public companies must disclose so much more than they used to do. Ethics codes, internal controls, accounting policies, work papers, and "report up, report out" are all new requirements created to make the governance of individual companies more apparent to the public.

5. Convergence in Responsibility

Both SOX and the CAAA make directors personally liable for their company's financial statements by requiring that they sign them to attest to their accuracy. As in all things, there are differences: Ireland requires directors, companies, and auditors to sign off on the accuracy of financial statements whereas the U.S. only requires executives to sign compliance statements.

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[234] Brian Hutchinson, The Companies (Auditing and Accounting) Act 2003 – An Overview, 11 Comm. L. Prac. 141, 143 (2004).
[235] Parma splat - Europe's corporate governance, Economist, Jan. 20, 2004.

Some have questioned whether this will hurt Ireland's position as an attractive location for foreign investment.[236]

VI. Conclusion

Convergence is necessary because Parmalat was not just an Italian problem, Ahold was not just a Dutch concern, and Enron was not just an American crisis. "The question is whether Europe's principles-based approach can endure."[237] The answer seems to be no: Europe is moving to a rules-based approach where government mandates the use of certain accounting standards and states regulate every aspect of the company.

Convergence would neither be total nor without critics. "America's rules are much more prescriptive and numerous. For example, the American ban on accounting firms providing some (but not all) non-audit work to audit clients, the certification of company accounts by company bosses and the requirement that a 'financial expert' (painstakingly defined by the SEC) be on each audit committee do not feature in the [E.U.] proposals."[238] Europeans have questioned the efficacy of some American ideas: "[r]otation of auditors--one of the more controversial measures introduced in July 2002 by the Sarbanes-Oxley act, America's response to Enron, WorldCom and other corporate scandals--seems to have been of little use [in Italy]."[239] Rotation of auditors may have been of little use in Parmalat, but we simply cannot know how many time bombs rotation has diffused.

On balance, the U.S. has the soft power to influence worldwide corporate governance and the E.U. has the hard power to converge its Members' laws. Through its legislative power to

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[236] PJ Henehan, Section 45 will kill Irish competitiveness, Irish Times, Feb. 25, 2005 ("In the opinion of a senior executive in an Irish subsidiary of a large US company that carries on a wide range of sophisticated activities employing hundreds of people in [Ireland], this section 'at the stroke of a pen makes Ireland uncompetitive'….The perception is that things have gone too far in the US. What is of concern is that the market perceives that Ireland has gone further than even the US.").
[237] More rules, Economist, Mar. 20, 2004.
[238] Id.
[239] Parma splat - Europe's corporate governance, Economist, Jan. 20, 2004.

regulate and direct Member law, the E.U. has streamlined European corporate law and governance. If its proposals and action plans are any indication, it plans to do more. Ireland is a prime example of the European move towards American-style rules-based governance.