FRENCH CORPORATE GOVERNANCE SYSTEM: THE CHOICE FOR THAILAND CORPORATE GOVERNANCE*

ระบบบรรษัทภิบาลของฝรั่งเศส: ทางเลือกของบรรษัทภิบาลในประเทศไทย

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Abstract

The possibility of transferring French CG system to Thailand is a very interesting topic, because Thailand and France share the civil-law system. However, the current adoption of UK CG Code is problematic because incompatibility of legal systems between Thailand and the UK. Moreover, British CG rules are designed to deal with dispersed ownership with well-established governance mechanism, so that they fail to address the issues of family-run business, ownership concentration, interlocking directorate, cross-shareholding, an informal alliance and state-owned enterprises (SOEs). Thailand uses the civil-law system, whereas the UK uses the common-law system. Hence, this paper explores this issue through literature review on French CG system, including corporate laws, ownership coordination and inter-firm coordination. After the exploration, it finds that stock markets in France and in Thailand are characterized by ownership concentration dominated by SOEs and family-run firms. However, French laws and regulators are less dispersed than Thai counterparts, because Thailand has too many CG-related laws and regulators. Hence, France and Thailand share the same legal system

* Received 23 June 2019; Revised 23 July 2019; Accepted 25 August 2019

and have similar business environment. For this reason, it recommends Thailand to reform its CG law on the basis of French CG system. To do so, Thailand should consolidate both CG-related laws and CG regulators for better enforcement and compliance. To do so, Thailand has to split its Civil and Commercial Code into a Civil Code and a Commercial Code, and then integrates related statues into the Commercial Code. To draft a Financial and Monetary Code, Thailand has to combine all finance and banking law together. Finally, it has to tie its CG rules with these codes.

Keywords: Corporate Governance, France, Choice

บทคัดย่อ

ในการนำเอาระบบบรรษัทภิบาลของฝรั่งเศสมาใช้ในประเทศไทยเป็นหัวข้อที่น่าสนใจ เพราะไทยและฝรั่งเศสใช้ระบบประมวลกฎหมายเหมือนกัน อย่างไรก็ตามการนำระบบบรรษัทภิบาลของอังกฤษที่ใช้อยู่ในปัจจุบันมีปัญหาเพราะระบบกฎหมายที่แตกต่างกันระหว่างไทยและอังกฤษ นอกจากนี้กฎธรรมาภิบาลของอังกฤษออกแบบมาเพื่อใช้กับการกระจายความเป็นเจ้าของในตลาดหุ้นที่มีกลไกการกำกับที่ดีจึงไม่ให้ความสำคัญกับเรื่องธุรกิจครอบครัว การกระจุกตัวความเป็นเจ้าของ การเป็นกรรมการข้ามบริษัทกัน การถือหุ้นข้ามบริษัทกัน พันธมิตรแบบไม่เป็นทางการและรัฐวิสาหกิจ ไทยใช้ระบบประมวลกฎหมายแต่อังกฤษใช้ระบบกฎหมายประเพณี ดังนั้นบทความนี้จึงสำรวจประเด็นนี้ผ่านการทบทวนวรรณกรรมของระบบบรรษัทภิบาลของฝรั่งเศส เช่น กฎหมายบรรษัท การประสานความเป็นเจ้าของและการประสานงานระหว่างบริษัท และพบว่าตลาดหุ้นของไทยและฝรั่งเศสจะมีการการกระจุกตัวความเป็นเจ้าของโดยธุรกิจครอบครัวและรัฐวิสาหกิจ เนื่องจากไทยและฝรั่งเศสใช้ระบบกฎหมายเดียวกันและมีสภาพแวดล้อมทางธุรกิจคล้ายคลึงกันดังนั้นบทความนี้จึงเสนอว่าไทยควรจะปฏิรูปกฎหมายเกี่ยวกับบรรษัทภิบาลตามแนวทางของฝรั่งเศส ซึ่งไทยควรรวบรวมกฎหมายเกี่ยวกับบรรษัทภิบาลและหน่วยงานบังคับใช้กฎหมายที่กระจัดกระจายอยู่เข้าด้วยกันเพื่อเพิ่มประสิทธิภาพในการบังคับใช้และปฏิบัติตามกฎหมาย ทำได้โดยแยกประมวลกฎหมายแพ่งและพาณิชย์ออกเป็นประมวลกฎหมายแพ่งและประมวลกฎหมายพาณิชย์ และนำประมวลกฎหมายพาณิชย์นี้ไปรวมกับกฎหมายอื่นๆที่เกี่ยวข้อง และไทยควรรวมกฎหมายที่เกี่ยวกับการเงินการธนาคารทั้งหมดมา

รวมเป็นประมวลกฎหมายการเงินการธนาคาร ก่อนที่จะนำกฎบรรษัทภิบาลไปผูกกับประมวลกฎหมายทั้งหลายเหล่านี้

คำสำคัญ: บรรษัทภิบาล, ฝรั่งเศส, ทางเลือก

Introduction

Corporate governance (CG) has been developed in Western countries, such as the US and the UK. Later on, it has spread through many countries around the world, including Thailand. Despite different legal systems between the UK and Thailand, Thai government chose to follow the English legal traditions for the country's CG (Krishnamurti, C. S., Sĕvić, A. & Sĕvić, Z. 2005) Because Thailand's legal system is largely based on civil law, the adoption of British-based CG system fails in Thailand. Moreover, British CG practices are largely based on dispersed ownership with well-established governance mechanism, they fail to address the issues of family-run business, ownership concentration, interlocking directorate, cross-shareholding, an informal alliance and to a lesser degree a pyramid of ownership and the structure of the board that are common in Thailand. The ownership of Thai firms is one of the most concentrated in East Asia (Peng, M.W., Au, K.Y. & Wang, D.Y.L. 2001) Thai ownership concentration is very similar to that in continental Europe, especially the French one, because family-run business and state-owned enterprises (SOEs) dominate stock markets, both in Thailand and France. Like Thailand, France uses civil-law system. As Thailand and France share the same legal system and have compatible ownership structure in stock markets, the adoption of French CG system is likely to work in Thailand. This adoption might be a better choice. Hence, this paper discusses French CG in terms of an overview, corporate laws, ownership co-ordination, inter-firm co-ordination and CG system. Then, it explores the possibility to transfer French CG system to Thailand. Afterwards, it ends up with conclusion and suggestion respectively.

Content

French CG

France established its first company in 1717 with the issuance of *billet d'état* (similar to nowadays government bond) (Murphy, A. 2005) French CG model is characterised by a high degree of ownership concentration in both family and state hands. Over the last three centuries, French family firms have had to rely on self-financing from retained profit as a capital market and banking structure has been weak since the failure of the banking system and stock market in 1720 (Murphy, A. 2005) Self-financing has been one of the main causes of ownership concentration. Another cause is the state intervention. French state has always played a major role in the economy since the days of Jean Baptiste Colbert (1619-1683), the controller general of finance (Murphy, A. 2005) The family ownership has frequently been subject to political criticism, but many families have continued to run business until nowadays. They have been viewed as the peers of management who help a middle manager to accomplish his or her job. French economy was traditionally dependent on family business. Since WWII, French economy has been dominated by large firms and the state (Hancké, B. 2001) because political and business elites cooperated to promote industry concentration and reconstruction (Maclean, M., Harvey, C. & Chia, R. 2010) French CG belonged to '*dirigiste*' model where the state dominated and sometimes intervened in the economy (Amable, B. 2003) (Hancké, B. 2001) If a French firm chooses a one-tier structure, its CEO and chairman tend to be the same person as *Président directeur-generale* (PDG). French firms in every corporate form are subject to corporate governance rules.

French corporate law

From 1700s to 1850 France had restricted corporate forms into only simple partnerships (*société en nom collectif*) and limited partnership (*société en commandite*). France enacted a law stipulating firms to have a two-tier board in 1856, and the Commercial Code and the Limited Liability Act (*Loi sur les société*) in 1867 incorporating this structure as it separated managerial and supervisory functions of the board (Aste, L.G. 1999) There was no corporate taxation before 1917, no formal rule of disclosure and no obligation to report corporate result before the 1930s (Gomez, P.Y. 2004) Hence, the autonomy of top management reached their peak during the inter-war period. During Nazi occupation, the Vichy regime abolished the two-tier structure in 1940 (Aste, L.G. 1999) However, the laws passed in 1940 and 1943 still required firms to have a unitary board of directors and to define the directors as independent management experts (Gomez, P.Y. 2004) France reintroduced a two-tier board in 1966, but it was not mandatory (Aste, L.G. 1999) Hence, French firms can choose either a unitary or two-tier board. The executive board makes decisions and manage firms under the CEO, and the supervisory board oversees these decisions and exercises control over the firms under the chairperson or PDG (Millet-Reyes, B. & Zhao, R. 2010) Only 1.62% of listed firms choose a two-tier structure (Aste, L.G. 1999) From 1986 to 1993 many state-owned firms were privatised. In 1995, *Viérot* Report recommended the good practices of CG (Gomez, P.Y. 2004) Since then, the state has privatised more large state-owned firms, such as Renault, France Telecom, but still keeps some stakes in the firms.

The main sources of corporate governance regulations in France include the EU Directives and Regulation relating to shareholders' right and information, the compulsory provisions of the French Civil Code, the French Commercial Code and The French Monetary and Financial Code, the General Regulation of *Autorité des marches financiers* (AMF = the French financial supervisory authority) and the recommendations issued by the AMF (www.amf-france.org) and the the European Security and Market Authority (ESMA)

(www.esma.europa.eu), the soft law recommendation of the corporate governance codes which later become mandatory statues enacted by French national assembly.

The French Commercial Code requires directors to serve *l'interêt social* (public stakeholders) by protecting the interest of the firms first and those of financial stakeholders and shareholders later. Their non-compliance led to criminal charge. The French Monetary and Financial Code stipulates listed firms to make information accessible to the general public subject to a regulation of AMF, but this regulation does not refer to particular CG code or report. However, AMF as the French securities and capital market regulator and ESMA jointly issue the recommendations in addition to AMF's General Regulation which is tied with the French Monetary and Financial Code. The French Commercial Code does not allow small shareholders to neither directly nor indirectly represent through the proxy voting system. (Hancké, B. 2001) Many large French firms have employee representatives in the board. (Maclean, M., Harvey, C. & Chia, R. 2010)

Code de Gouvernance d'Entreprise is published by *Association Française de la Gestion Financière* (AFG) (www.afg.asso.fr). Financial Security Law of France (*Loi sur la Securité Financière*) is a French equivalence to Sarbanne-Oxley Act enacted in 2003. French CG code governs *société anonymes* (SA) or public limited company with both a unitary and a two-tier boards and partnership. It refers to Community law and the French Commercial Code. The French Commercial Code provides an option between a unitary formula and a two-tier structure. It requires representation of women, employees with more than 3% shareholding, and work council in the boards. French Code stipulates the duration of directors. Auditors are statutory. It requires separation between CEO and chairman as this practice is new in France. This CG code requires top management to embrace more shareholder value as new foreign investors participate (Morin, F. 2000)

Ownership coordination in French firms

In the French turbulent history, many wars and upheavals have undermined the development of banking system and stock markets. This development is quite late in comparison with the same development in the UK, the US and the Netherlands. This development completed in 1966 when French banks flourished (Murphy, A. 2005) From 1895-1914 many French firms were reluctant or sometimes hostile to use banks and stock markets to raise capitals. A change in inheritance laws in 1905 led to shift from self-financing to debt-financing. Family ownership had long been embedded in France before WWII. From 1945-1982, there had been waves of nationalisation. Since 1982, Chirac government have privatised state-own enterprises (SOEs), so that the number of French shareholders increased from 1.7 million in 1982 to 6.2 million in 1987.

The majority of the large firms are family-owned and the state holds large minority block in many newly privatised firms (Aste, L.G. 1999) (Hancké, B. 2001) From 1992-1998, 57% of listed had individuals or families who own more than 10% stake A third of listed firms were widely held. Another third were founder-controlled firms and the leftover third were heir-controlled family firms. In 2001 around 40% of unlisted firms have individual shareholders who held more than 50% stake. Block holders often hold around 30% stakes with controlling vote for *Cotation Assistée en Continu* (CAC) 40 firms (Murphy, A. 2005) In 2005, the state still held 33% stake in leading firms in the Paris Bourse.

Nowadays, most French public companies adopt the corporate form of a *société anonyme* (SA) with roughly 90% of *Société de Bourse Française* (SBF) 120 (the index of the 120 largest firms listed on Euronext Paris) (www.boursier.com). Some French listed firms adopt the form of a European company (Societas europaea = SE) governed by European regulation which are not discussed here (eur-lex.europa.eu). Other listed firms adopt the form of a *société en commandite par action* (SCA) as they are family-run firms. In the

SCA, family owners and founders are often unlimited liability partners, whereas other partners are limited liability shareholders. The SCA has an efficient defence mechanism against unsolicited (hostile) takeover. Hence, a weak bank system and capital market led to the formation of holding companies. (Murphy, A. 2005) The state still supports some strategic decisions of these firms and continues to exercise some control and encourage domestic monopoly (Yoo, T. & Lee, S.H. 2009) Hence, ownership in French firms is highly concentrated and generally owned by a small number of investors. The firm founders often retain majority shares.

Inter-firm coordination in France

France is more open to foreign investors than German. *Caisse des Dépôts et Consignation* stabilises shareholding base of French companies. (Morin, F. 2000) Around 40% of the market capitalisation of the top-40 firms listed on CAC was tied up in cross-shareholdings in the late 1990s. (Hancké, B. 2001) In 2002, *Mouvement des Entreprises de France/Association Française des Entreprises Privée* (MEDEF/AFEP) tried to reform CG. The MEDEF/AFEP have set up the *Haut Comité de Gouvernement d'Entreprise* (HCGE) as a governance committee in charge of verifying the implementation of and compliance with their code which is based on 'comply-or-explain' principle (afep.com). Their attempt failed to reduce reciprocal directors' mandates and cross-shareholding. Multiple board membership still exists and fostered cohesive tied for the elites. The financial deregulation has led to elite-controlled cross-shareholding instead of shareholder capitalism because banks cannot monitor new CG effectively.(Hancké, B. 2001) The cross-shareholding exits in France whereby one friendly firm hold majority shares of each other (*noyaux durs*) like in Japan and South Korea. (Aste, L.G. 1999) However, the cross-shareholding has been declining, though continuing to have a role. (Morin, F. 2000)

Because France has strong elite networks with state activism (*dirigiste* approach), interlocking directorates are common. As most top executives, civil servants and politicians graduate from *Grande école*, elite-based coordination mechanism is the main characteristics of *dirigiste* model with concentrated power relations and state initiative policy. (Maclean, M., Harvey, C. & Chia, R. 2010) As efficient coordination mechanisms for French CG, the elite networks and state ownership facilitate interlocking directorates. Because French firms often recruit senior managers directly from civil service, this recruitment enhances close relations between the state and firms. Many top executives used to be bureaucrats. Consequently, French boards are notorious for political representation and the state often muddles in firms' strategic decisions. (Balachandran, K. R., Rossi, A. & Van der Stede, W. A. 2011) Hence, most French CG research is orientated towards underscoring the political dimension of management. (Gomez, P.Y. 2004)

French CG system

Before the 1990s, French CG had been bank-based. State-owned banks or firms have been used for public intervention in the economy. Many French firms, such as LVMH, Kering and Carrefour that adapt a two-tier board system are more successful. However, this system cannot eliminate interlocking directorates, but allow both directors from the executive board (*Conseil d'executive*) with mandatory resignation to be appointed to the supervisory board (*Conseil de surveillance*), and the old directors tend to use the supervisory board to retain their control for political, not economic reason. (Millet-Reyes, B. & Zhao, R. 2010) Since 2000, a new CG structure which relied more on outside director has replaced the closed CG model. French CG has no longer been organised around either banks or the state. The new long-term institutional investors, such as pension funds have been patient for long-term capital. The management of large firms are independent from outside

influence through complex cross-ownership arrangement. (Hancké, B. 2001) Hence, the financial market cannot discipline French management. Double voting right can be included in firm charters under certain conditions, and can be revoked by a share transfer as anti-takeover mechanism. (Morin, F. 2000) With higher dividend non-voting shares exit.

Nevertheless, to attract more foreign investors, some private firms try to extricate themselves from this practice. The call for transparency, control and clearly defined accountabilities dilutes the autonomy of executives. Almost half of the most powerful French directors combine the role of chairpersons and CEOs as PDGs enjoy discretion in parallel with the state's restructuring policy in spite of increasing pressure from foreign investors and independent directors. (Maclean, M., Harvey, C. & Chia, R. 2010) French top executives often argue that autonomy is a necessary condition for restructuring. They prefer stability and continuity of membership within the boards, maintained by interlocking directorates. To concentrate on profitability, autonomy from the state and other stakeholders is necessary to exclude a broad social and political dimension from strategic decisions. (Hancké, B. 2001) Thus, minority shareholders are not well protected.

Conclusion

Like Thailand, family-run business and SOEs dominate French stock market with a high degree of ownership concentration. Political and corporate élites collude to promote industry concentration and reconstruction. French CG is characterized by 'dirigiste' model where the government guides the economy. Since *Viérot* Report recommended the good practices of CG in 1995, France has developed its CG from the EU directives, the mandatory provisions of the French Civil Code, the French Commercial Code, the French Financial and Monetary Code, regulation of AMF and ESMA financial regulator and some

soft law recommendations. French Commercial Code mandates directors to serve public stakeholders, including firms, financial stakeholders and shareholders. If they fail to comply with the code, they will face criminal charge. *Code de Gouvernance d'Enterprise* and Financial Security Law were among the first CG-related laws in France.

Like in their Thai counterparts, ownership in French firms is highly concentrated and generally owned by a small number of investors, mainly founders, the state and family members. However, France is more open to foreign investors than Thailand. Like in Japan and South Korea, the cross-shareholding and interlocking directorates are widespread in France. Like in Thailand, French firms often invite ex-bureaucrats to join their boards.

French Commercial Code allow firms to choose either a unitary and a two-tier board system, but Thai corporate law does not require Thai firms to adopt any particular board structure. Like in Thailand the financial market cannot discipline French management. Like their Thai counterparts, French top executives believe in their discretion for any strategic decision-making. They prefer stability and continuity of membership within the boards. Therefore, it is more sensible to adopt French CG rules in Thailand as legal system and business environment in both countries are quite similar.

Suggestion

The main problems of Thai CG system are: 1) incompatibility between UK CG Code and Thai legal system, 2) too many laws related to CG, and 3) too many regulators. The current Thai CG Code adopted directly from the UK with different legal systems and business environments does not work properly in Thailand. The UK uses Common-law system whereas Thailand uses Civil-law system. This adoption has many flaws because the UK system lacks legal sanction and clear punishment when stock market commission as a regulator enforces listed companies to comply with CG code.

Thai government and legislators should look to the CG system in the countries that are more compatible with Thai business environment, rather look only to the US or the UK with different business environments and legal systems as the sources of updating Thai commercial law. In compatibility with the civil law that Thailand adopted from continental Europe, including France for a century, Thai legal experts and legislators should draft Thailand's CG code with more compulsory nature like in France whose environments are more similar to those of Thailand. The researcher sees that France uses Civil-law system like Thailand. Thailand should adopt French CG system because both family-run firms and SOEs dominate both Thai and French stock markets with ownership concentration is a norm.

As in France, the enactment of statutory regulation that either integrate or link CG code into Thai Commercial and Civil Code are more in line with the civil law in France, but some Anglo-Saxon law can be used if it promotes business and attract investors. However, Thailand may require SET, BOT, SEC, OIC etc. to draft and update CG code modelled on France CG code and enacts laws to link this code to Thai Commercial and Civil Code, because France CG code is updated regularly and the tie-up between this code and Thai Commercial and Civil Code follows the way France does in its civil law. British CG code allows debates before punishment while the French CG law can prosecute the wrongdoers faster. Even if well-structured boards cannot always preclude questionable corporate actions, the compulsory CG rule can facilitate legal actions in Thailand.

More than 30 statues in Thailand concerning CG confuse company directors and regulators. Some laws impose criminal penalties on director and non-director managers of companies on the one hand, and others allow SET and shareholders to file civil lawsuits against these managers on the other hand. Many directors in its training courses complained that scattered laws governing the role and responsibilities of directors are confusing. The laws

governing CG are unclear, diversified and too complicated. CG laws should require qualification of directors, duty of the chairman. The two-tier board can prevent duality between CEO and the chairman, conflict of interest and collusion. As Thai companies face the problem of different interpretations on CG rules from various regulators, Thailand needs minimum legal requirement for CG. The law must deal with inter-firm loan, corporate corruption and the misuse of corporate fund. More than 50% of independent directors are needed. Thai government and legislators should draft the specific corporate law to govern all aspects of listed firms as they involve many stakeholders, such as shareholders, family founders, staff and so on. The well-written law will reduce different interpretations on CG by several regulators. Even if the regulators cannot be merged for the time being, all of them must interpret the same rules in the same way.

To follow French CG system, Thailand should split Civil and Commercial Code into Civil Code and Commercial Code. Then, it combines Commercial Code with Public Limited Companies Act 2551BE, Social Enterprise Promotion Act 2562BE, Cooperative Act 2562BE, Small and Medium-size Enterprise Promotion Act 2561BE and other related statues so as to create a new commercial code which covers all forms of enterprises. This new code may create a new corporate form similar to French SCA to protect Thai family-run listed firms from unsolicited takeover in Thailand's stock market. Thailand should create a monetary and financial code through combining Financial Institution Act 2561BE, Bank of Thailand Act 2561BE, People's Financial Institution Act 2562BE, Commercial Banks 2505BE, Insurance Commission Act 2550BE, Security and Exchange Act 2535BE and other related statues. Thailand should tie its CG Code with these codes in order to improve legal sanctions of corporate governance. French CG rules are tied with the existing codes and less dispersed than Thai CG rules which are written in Civil and Commercial Code, several acts and statues and SEC rules. Thai CG rules causes

a lot of problems for board of directors to comply with. French CG rules clearly state the relationship between shareholders and executives in corporate governance and prosecute the wrongdoers faster than either current Thai or UK CG rules.

(Segrestin, B. & Hatchuel, A. 2011) believe that the current corporate laws in the world do not protect the autonomy of management. The management theory and CG literature has underestimated the role of law in the evolution of CG, especially in European countries. They suggest new governance rules to ensure the executives' freedom to pursue efficient and legitimate, strategy and goal. The best form of CG should strike a balance between protecting minority shareholders' right and ensuring managerial discretion. They recommend three legal principles: 1) the parties who recognise the authority and accept that their potential is managed for the success of the corporate strategy should be differentiated from the other stakeholders, 2) they should be authorised to appoint and dismiss executives, but not to give incentive that can distract executives' attention from corporate survival, 3) they should contribute jointly to the impact of strategic decisions. The legislators should pass the law to regulate corporate behaviours, executives and shareholders to ensure the protection of all stakeholders. Their suggestion can help Thai legislators to consolidate many Thai statues relevant to CG for more efficient interpretation and enforcement. Thailand may need to adopt US tough regulation like the Sarbanne-Oxley Act as the aftermath of Enron (Nowland, J. 2008), but integrates it into the corporate law. As the corporate laws need to be updated, the institution like Council of the State may help Thai legislators and government to update and consolidate the current corporate laws, and draft the new ones if necessary.

There are too many regulators in Thailand and each of them has different rules and interpretations. As Thai companies face the problem of different interpretation of CG rules from various regulators, Thai government

and legislators should consolidate several regulators that have similar function and rules. Nowadays Thailand has many regulators that enforce CG practices in different industries. For instance, BOT enforces these practices for banks. OIC does it for insurance companies. Thai companies are sometimes confused. Hence, Thai legal experts and legislators should design institutions for consolidating uncoordinated regulations that lead to poor CG enforcement in Thailand. For example, Thailand should have nation-wide CG practices designed jointly by BOT, OIC and SEC, before integrating BOT's supervisory division with OIC. The separate role between SET and SEC must be clear-cut and all CG practices must be recommended by SEC as a regulator, not by SET. Afterwards, the CG for special business, such as banks, insurance will be designed as affixed to the nation-wide CG practices. To improve its financial supervision, Thailand has to separate financial supervisory function from Bank of Thailand (BOT), so that BOT can focus mainly on monetary policy. Then, it incorporates financial supervisory function into Office of Insurance Commission and creates a new financial supervisory agency. To reduce confusion among Thai firms, Thailand has to reorganize and consolidate several firm regulators which report to several ministries, such as Ministry of Commerce, Ministry of Interior Affairs, Ministry of Agriculture and Cooperative into one regulator.

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