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Corporate Governance and Communications Transparency in the DaimlerChrysler Post-Merger Era

Robert LoBue
Reutlingen University

Abstract. This case study concentrates on comparing the German and U.S. corporate governance systems using the recent experiences of DaimlerChrysler AG and its chairman, Jürgen Schrempp, as reported in the international business press to illuminate differences in investor relations communications practices, in particular. The recent experience of DaimlerChrysler, because of its highly visible role as a "trailblazer" in the U.S. financial markets and due to the difficulties it has encountered, presents an excellent example for analysis of the governance issues inherent in a German-American direct foreign investment situation. Gaining a better understanding of the problems encountered by DaimlerChrysler should allow European business leaders to proactively design their own communications strategy including identifying potential pitfalls for their firms. Without this understanding, European firms could be discouraged from continuing to take advantage of the benefits of international financing and investment available from capital sources in U.S. stock and bond markets and business expansion opportunities in the U.S. product and service markets.

Keywords: corporate governance, investor relations, shareholder lawsuit, DaimlerChrysler, disclosure and transparency, merger of equals, board of directors.

1. The DaimlerChrysler "Merger of Equals"

1.1. Current Situation

In early 2003, the world business press reported on the dramatic financial and operational turnaround of the Chrysler Group of DaimlerChrysler AG under the leadership of German executive Jürgen Schrempp, chairman of DaimlerChrysler.[1] After six consecutive quarters of operating losses totaling about $3.5 billion, excluding one-time charges, Chrysler announced that it had finally achieved an operating profit in all four quarters of the prior calendar year, totaling over $1.3 billion. However, the press simultaneously reported that a "Time Bomb" threatened DaimlerChrysler's future results.[2] A $1 billion lawsuit brought against DaimlerChrysler executives by its third largest shareholder, American "corporate raider" Kirk Kerkorian, Chrysler

1. Alex Taylor, "Just another sexy sports car? Sure. But it's also a whole new way of doing business at Chrysler", Fortune Europe Edition, Vol. 147 No. 5, March 17, 2003, pp. 30-33.
2. Dietmar Hawranek, "Zeitbombe in Delaware", Der Spiegel, 12/2003, pp. 84-86.

Corporation's largest investor from the pre-merger period, was scheduled to come before the U.S. federal court in the state of Delaware.

This situation has been portrayed, as shown below, by the editorial cartoonist of a major newspaper serving the Detroit metropolitan area, home of DaimlerChrysler's American headquarters at Auburn Hills, Michigan.[3] Although the challenge of the Kerkorkian caricature on the left side of the cartoon is genuinely playful and humorous in its outlook on the situation, the box on the right forebodingly suggests a serious entrenched incompatibility of German and American business cultures. The efforts of creating a single corporate culture in one of the world's largest enterprises after years of post-merger integration activities are apparently at risk of being undermined by national allegiances and incompatible styles.

1.2. Expectations and Fall-Out of Merger-Related Events

Following a very turbulent period of at least a dozen years where the company found itself twice on the brink of financial disaster, by the mid-1990's Chrysler had developed into what many industry watchers considered the most profitably run company in the American automobile industry. Chrysler had

3. Mike Thompson, Detroit Free Press, November, 2000.

invented the minivan concept with its highly successful Dodge Caravan and Plymouth Voyager models in the USA and created the sport utility vehicle (SUV) category with its Jeep division (obtained in its 1980's acquisition of AMC – American Motors Corporation). Chrysler had far less success, however, with its standard family oriented automobile brands, a weakness that still left it vulnerable to acquisition. In 1995, Mr. Kerkorian launched a takeover attempt through his investment firm, Tracinda, which was rebuffed by Chrysler's board of directors and management under the leadership of chairman, Robert Eaton.

Also in 1995, representatives from Daimler-Benz AG, headquarterd in Stuttgart, Germany, whose new chairman was Mr. Schrempp, met with Chrysler to explore the possibility of a merger between the two companies. Daimler-Benz, like Chrysler, enjoyed one of the industry's highest rates of profitability stemming from its worldwide reputation of excellence in engineering and production of its high quality mid-size and full-size Mercedes-Benz luxury sedans. Daimler-Benz was planning for the introduction of a new line of more affordable family sedans, the 'A' series, and for a new mini category concept, the 'smart' car, in Europe. In anticipation of the widely predicted consolidation of automobile industry competitors worldwide,[4] Mr. Schrempp became concerned about Daimler-Benz' limited future if it could not achieve substantially greater economies of scale.

In the same year, the Private Securities Litigation Reform Act of 1995 was enacted. The legislation was a major corporate governance event in the USA, amending both the Securities Act of 1933 and the Securities Exchange Act of 1934. The new law intends to protect executives by providing a "safe harbor" to those who make "forward-looking statements" about impending transactions from frivolous lawsuits based solely on the fact that future results differ from expectations set by those statements. It encourages company managers like Mr. Schrempp to be open in disclosures and to favor transparency when discussing material events, such as impending mergers, by defending them from having their own honest and forthright statements from being used later against them maliciously in court.

Following three years of off-and-on meetings spanning from preliminary discussions through detailed negotiations, in 1998, Mr. Schrempp and Mr. Eaton announced their intention to merge their businesses through an exchange of stock. They promoted this monumental event as the largest merger transaction of two organizations in industrial history,[5] with the main strategic vision of becoming no less than the largest player and the clear leader

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4. Ralf P. Brammer, "Erfahrungen mit Investor Relations eines internationalen Konzerns am Beispiel der DaimlerChrysler AG", Die Praxis der Investor Relations, Klaus Rainer Kirchhoff and Manfred Piwinger eds. – Neuwied, Kriftel: Luchterhand, 2000, p. 256. In 1960 there were 42 automobile manufacturers worldwide, by 1998 there were only 17, with signs of further consolidation coming.

in innovation in the worldwide automotive sector. To illustrate the total size of the proposed merged entity and relative sizes of the two companies, the following pre-tax pro forma statement of income (profit and loss) has been summarized from information that was presented in the merger prospectus.

DAIMLERCHRYSLER AG
UNAUDITED PRO FORMA STATEMENT OF INCOME
For the Year Ended December 31, 1997
(in millions)

	Historical		Pro Forma	Pro Forma
	Daimler-Benz	Chrysler	Combined	Combined
Revenues....................	DM 124,050	DM 105,205	DM 229,255	$ 127,131
Cost of sales	(98,943)	(84,879)	(183,822)	(101,936)
Gross margin	25,107	20,326	45,433	25,195
Selling/admin/other expenses	(17,433)	(9,703)	(27,136)	(15,048)
Research and development	(5,663)	(2,972)	(8,635)	(4,788)
Other/financial income...	2,238	251	2,489	1,380
Income before income taxes....	4,249	7,902	12,151	6,739

Notes: Currencies are DM = German Marks and $ = U.S. Dollars. Pooling of interests assumed.
Source: Chrysler Corporation Proxy Statement/DaimlerChrysler AG Prospectus, 1998, p.110.

In April, 1998 the law on control and transparency in business (known as the "KonTraG"[6]) was enacted in Germany, supplementing previously introduced related legal initiatives including the German Stock Corporation Act, German Securities Trading Act, German Commercial Code, German Antitrust Act, and the German Banking Act. The German Panel on Corporate Governance was satisfied that, "The essential points of the OECD Principles of Corporate Governance ... are covered..."[7] by this body of law. For a number

5. "The Merger of Daimler-Benz and Chrysler", http://www.daimlerchrysler.com/investor/merger/merger_e.htm, 1998, p. 1.
6. "Control and transparency in business (KonTraG): Corporate governance reform in Germany", www.bmj.bund.de/misc/e_kont.htm, 1998, pp. 1-5.

of years the Organization of Economic Cooperation and Development (OECD) had openly debated and drafted a set of non-binding, but strongly recommended set of corporate governance principles "to provide guidance and suggestions for stock exchanges, investors, corporations, and other parties that have a role in the process of developing good corporate governance... [which] should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders and should facilitate effective monitoring, thereby encouraging firms to use resources more efficiently."[8]

In September of 1998, the shareholders of both Daimler-Benz and Chrysler, including Mr. Kerkorian who through Tracinda still held over an 11% interest in Chrysler,[9] voted overwhelmingly to approve the transaction, after assurances from the two chairmen that the governance structure of the new entity would be a "merger of equals". In this spirit, Mr. Schrempp and Mr. Eaton, agreed to share the office of chairman in the new company, which was named DaimlerChrysler AG.[10] Major roles and responsibilities were allocated among board members of both pre-merger companies and between executives in Stuttgart and Auburn Hills. All shares in both corporations were exchanged for entirely new DaimlerChrysler AG ordinary shares. These new shares were, in turn, simultaneously listed and traded on the New York Stock Exhange, the Frankfurt Stock Exchange, and various other exchanges around the world, becoming what has been termed the first truly global shares.[11]

After only one year, Mr. Eaton resigned in 1999, leaving Mr. Schrempp as the sole chairman. It was reported that Mr. Eaton, after announcing his departure, defended his involvement in supporting the merger decision curiously "saying he didn't want to have to lead another 'comeback'. He clearly saw that industry trends were working against the company."[12] This raises the question whether Mr. Eaton's fears were general, concerned with Chrysler's long-term prospects in a consolidating industry, or whether they were specific, aware of Chrysler's short-term issues in its internal business operations that were not known by Mr. Schrempp nor the public.

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7. German Panel on Corporate Governance, "Corporate Governance Rules for Quoted German Companies", January 2000, pp. 1-9.
8. OECD Principles of Corporate Governance, SG/CG(99)5, www.oecd.org/daf/corporate/principles.htm, April 16, 1999, p. 2.
9. "Chrysler Corporation Proxy Statement/DaimlerChrysler AG Prospectus", (combined document), http://www.daimlerchrysler.com/investor/merger/book.pdf , August 6, 1998, p. 125.
10. "Chrysler Corporation Proxy Statement/DaimlerChrysler AG Prospectus", 1998, p. 93.
11. Ralf P. Brammer, 2000, p. 268. According to the author, prior to this listing of ordinary shares, German firms had only listed their shares on the New York Stock Exchange as American Depository Receipts (ADR's) or American Depository Shares (ADS's).
12. Holman W. Jenkins, Jr., "The Limits of Schremppism", The Wall Street Journal Europe, December 7, 2000, p . 8.

During 2000, indications that Chrysler was struggling began to surface. Mr. Schrempp publicly declared in September that he expected results would turnaround positively in the fourth quarter. The next day after his statement, he was apparently embarrassed by an announcement by U.S. Chrysler managers that seven factories would be closed for one week due to oversupply in inventory.[13]

Before the end of the year, Mr. Schrempp found himself in the midst of substantial investor pressure and unfavorable media publicity stemming from more surprising news from Chrysler. In the third quarter of 2000 alone, the Chrysler business unit had, with little warning, incurred operating losses of close to $500 million. A similarly dramatic loss of confidence by the investment public was evidenced by a greater than 50% decline in the share price of the combined company to 51 EUROS from 108 EUROS at its post-merger peak.[14] Apparently unaware of the full extent of additional impending fourth quarter operationg losses of the Chrysler unit ($1.4 billion) to be exposed only a few weeks afterwards, but nevertheless dismayed by the performance of the unit under its soon to be vacated American senior management team,[15] Mr. Schrempp made the following revelation in an interview with the Financial Times:

> 'Me being a chess player, I don't normally talk about the second or third move. The structure we have now with Chrysler [as a standalone division] was always the structure I wanted,' he says. 'We had to go a roundabout way but it had to be done for psychological reasons. If I had gone and said Chrysler would be a division, everybody on their side would have said: 'There is no way we'll do a deal'…But it's precisely what I wanted to do. From the start structure, we have moved to what we have today.'[16]

It should not be difficult for the public to understand that Mr. Schrempp's statements were made in an emotional time, where frustrations could reasonably lead to an attempt to rationalize the very real original intention of a "merger of equals" strategy. These frustrations were borne from the major surprises of the size of the unfavorable financial results and the significance of the operational performance problems at Chrysler. Was Mr. Schrempp genuinely unaware of the magnitude of the problems at Chrysler? It can be reasonably assumed so by a memo written by James Holden, president of

13. Edmund L. Andrews, "Chrysler's President Expected to be Replaced by German Executive", International Herald Tribune, Novermber 15, 2000, p. 15.
14. Tim Burt & Richard Lambert, "The Schrempp Gambit", Financial Times, www.ft.com, October 30, 2000.
15. Susanne Preuß, "DaimlerChrysler May Oust Key U.S. Officer", Frankfurter Allgemeine Zeitung, English Edition, No. 188, November 15, 2000, p. 5: "There are now only two Americans on the twelve-person management board: Thomas Sidlik and Gary Valade, who are both responsible for purchasing."
16. Tim Burt & Richard Lambert, 2000.

Chrysler Corporation, to his own managers at the Chrysler unit the day after the Financial Times published the interview with Mr. Schrempp. In the memo Mr. Holden is reported to have warned, "'Further negative surprises would erode my credibility on the board of management.'"[17] Mr. Holden, therefore, was himself not able to inform his boss, Mr. Schrempp, of the issues at hand in a timely manner. In November of 2000, Mr. Holden was replaced by former Daimler-Benz exectutive Dieter Zetsche.

Perhaps if Mr. Schrempp had some experience playing the American card game of poker, along with chess, he would have been inclined to follow the long recommended strategy of never showing one's hand once the opponent has folded. He then certainly would not have delivered such potentially damaging evidence as the Financial Times quote into the hands of Mr. Kerkorian, DaimlerChrysler's third biggest shareholder with about 3% of total shares. As reported in the international business press, in the lawsuit filed on November 27, 2000 against DaimlerChrysler AG, "Kerkorian …charges that…Schrempp and three other German DaimlerChrysler executives…deliberately misled the public about the aims of the merger. Instead of a 'merger of equals,' as Mr. Schrempp called it, Daimler-Benz's 'true intention was to acquire and subjugate Chrysler, reduce it to division status and fire Chrysler's management….'"[18]

At the close of 2000, Chrysler dealers in Germany were very concerned about the future of their business prospects and publicly voiced their surprise and dismay with the situation at DaimlerChrysler. The dealers criticized specifically the abrupt handling and cancellations of their dealer contracts.[19] They also had begun to find fault with DaimlerChrysler executives who they claimed had wasted time following the merger, apparently causing Chrysler to shift its product direction and slip its market position.[20] Both of these dealer issues could arguably be linked to change of control and the disguising of management's strategic intentions at the time of the merger.

Chrysler's suppliers, if not managed appropriately, also showed signs of chafing under the apparently one-sided pressure recently being placed on them from Chrysler's new German president, Mr. Zetsche. In early December of 2000, suppliers were notified that Chrysler expected to reduce supply chain costs by 15% over two years and that a 5% reduction of supplier prices would be needed immediately (in effect on January 1, 2001). Previously, the general

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17. Susanne Preuß, 2000, p. 5.
18. John Schmid, "Daimler Chief Under Fire", International Herald Tribune, No. 36,621, November 29, 2000, pp. 1 & 18, p. 18.
19. Harry Pretlaff, "Viele Chrysler-Händler sind schockiert", Stuttgarter Zeitung, No. 279, December 2, 2000, p. 14.
20. Harry Pretlaff, "Zeit verloren: Streit um Chrysler-Vertrieb", Stuttgarter Zeitung, No. 279, December 2, 2000, p. 14.

expectations of both Chrysler and its suppliers were that price cuts should average about 3% to 4% on an annual basis.[21]

The difference in the manner that these price cuts had been communicated to Chrysler's suppliers, most of them from North America, compared to the manner of communication that Mercedes-Benz uses with its suppliers, most of them from Europe, is at least as dramatic a message, if not more so, as the targets themselves. Mercedes-Benz manages cost reductions as a joint development effort between the Mercedes-Benz and supplier teams. Under a formal program called the "Tandem-Model", savings that result from the efforts of the joint teams are shared with the suppliers, not demanded in total from them.[22] Perhaps this is why the response of an executive of Delphi, one of Chrysler's largest auto parts suppliers, to the call for these drastic cuts contained such carefully selected phrases as "relationship in place", "working closely together", and "mostly earned in the interests of both sides".[23] Chrysler's suppliers are likely to be just as sensitive to any indication of differences in treatment of the Chrysler operations by the former Daimler-Benz executives as investors or dealers would be.

Also at the close of calendar year 2000, perceptions of differences in treatment and even suspicions of profit expropriation had unfortunately also been voiced by Chrysler employees. They were fully aware that Chrysler had been a highly profitable automaker on its own and were now openly questioning how these profits could so quickly have disappeared. They also were expecting DaimlerChrysler's executives to provide some sort of public reckoning. In the words of one factory worker directed at Mr. Schrempp, "'Jürgen should tell the people where all the money went.'"[24] This sentiment should not be easily dismissed as a voice of dissent of a single employee, because Chrysler rank-and-file employees in the U.S. are represented collectively by the United Auto Workers union.

21. N.N., "Chrysler setzt Zulieferer unter Druck", Stuttgarter Zeitung, No. 285, December 9, 2000, p. 14.
22. Michael Heller, „Kein Tandem: Zetsches Einstand bei Chrysler", Stuttgarter Zeitung, No. 285, December 9, 2000, p. 14.
23. N.N., "Chrysler setzt Zulieferer unter Druck", 2000, p. 14.
24. Harry Pretzlaff, "'Die bange Frage lautet: Verliere ich meinen Job?' ", Stuttgarter Zeitung, No. 285, December 9, 2000, p. 13.

2. Applicability of the OECD Principles of Corporate Governance

2.1. The Challenge of Communication

The DaimlerChrysler crisis has been blamed on cultural incompatibility, in other words, a clash of American and German business cultures. However, it is shown above that not only Mr. Schrempp had created issues with his statements regarding his original intentions of the merger strategy. Mr. Eaton, also, has given the impression that he was not actually looking for a "merger of equals", but more of a "white knight" to save Chrysler from another potential financial disaster. Mr. Holden, as well, indicated that Chrysler's management team may have suffered from its own issues of vertical communication within its chain of command and control.

From these confusing communications, U.S. investors appear to have acquired the feeling that they were holding equity or debt of a functionally different organization than the "merger of equals" presented to them by Mr. Schrempp. In general, U.S. investors and other stakeholders are on the alert for and prepared to penalize activitities which amount to expropriation of funds or of other assets by foreign companies and individuals raising funds or making acquisitions in the U.S. market. Expropriation does not have to be a direct misappropriation of cash, fraud, nor other malfeasance. It can take the form of a change in strategy which leads to a different organizational or investment profile for the company than what was publicly communicated at the time of a merger, acquisition, or stock or bond offering.

Mr. Schrempp's interview statement in the Financial Times could certainly have been meant as an admonition of Chrysler management regarding their own poor performance and serious lack of communication, as well as a foreshadowing of the tough corrections he will have to require of them as a result. In this case, the safe harbor legislation rightly protects his decision to change strategy from a "merger of equals" to a divisional structure for Chrysler. However, based on his unfortunate selection of words, or the Financial Times interpretation thereof, his statement held the appearance of an admittance of original intentions, quite different than the plans documented and communicated to shareholders and the general public at the time that shareholders of both corporations were asked to approve the merger.

High profile strategies such as cross border mergers and acquisitions with U.S. companies and parallel listings of shares in U.S. stock exchanges have been employed by European corporations with increasing frequency. However, the DaimlerChrysler situation demonstrates that these strategies present significant corporate governance challenges which must be planned for and addressed by company directors and executive management to avoid potential setbacks and failures. It is critical that these international business leaders are aware of the structural and cultural differences of the corporate governance system in the U.S., especially as compared to the practices generally accepted in their home country, for example, Germany. They can use this information, and the experiences of Mr. Schrempp with Chrysler, to check their own behaviour in relation to public announcements and statements in press releases, speeches, interviews and other disclosures.

The OECD Principles of Corporate Governance which were published in final form in May of 1999 can be used as a framework for analyzing the German-American business environment. The OECD intended that the principles provide direction to the corporate officers and board members as well as function on their behalf. They encourage them to pursue self instruction, self assessment, and self enforcement[25] and to work with national governments in designing regulations appropriate for the local business and economic situation. It is intended that compliance with these principles by corporate actors along with complementary national laws and regulations operating under effective monitoring and fair judicial systems, will reduce investor and stakeholder grievances, like those of Mr. Kerkorian, and, in turn, limit the need for them to pursue legal remedy through litigation.

The OECD principles are divided into five major categories which can provide guidance in the DaimlerChrysler situation:

I. The rights of shareholders
II. The equitable treatment of shareholders
III. The role of stakeholders in corporate governance
IV. Disclosure and transparency
V. The responsibilities of the board

Researchers have uncovered contemporary structural evidence of national differences in the financial and institutional market structure in the U.S. versus in Germany applicable to each of these categories. Together these can help to explain the difficulty of adjustment facing most German executives like those at DaimlerChrysler to the systems of corporate governance in the U.S. as well as in the KonTraG legislation regulations and the OECD principles in general.

2.2. OECD Principle I. The Rights of Shareholders

In their landmark 1932 studies *Power without property: The rise of the modern corporation* and *The modern corporation and private property*, researchers Berle and Means showed that managers of most major

25. OECP Principles of Corporate Governance, 1999, p. 3.

corporations would have varyingly different objectives for the business under their control than would be required by the widely dispersed shareholding owners of the businesses themselves.[26] This idea is known as "agency theory" in recognition of managers' responsibilities as agents employed on behalf of the owners of the business. The OECD, therefore, states that it develops and updates "the Principles [to] focus on governance problems that result from the separation of ownership and control."[27]

Financial institutions are able to protect their direct commercial lending and private equity interests through the confirmation of detailed, professionally drafted and negotiated legal contracts. These contracts formalize the repayment and ownership provisions of these investments. They provide also for mechanisms of recourse and liquidation for the institutions in the case of default or premature divestiture, respectively. While the former is the desired and most often accomplished outcome, resulting from the due diligence processes that professional financial services firms employ, the unfortunate latter outcome is a measured risk that the institutions accept as one of the costs of operating in the debt and equity markets. In a comparable manner, publicly traded debt and equity financial instruments ("securities") carry covenants and provisions that detail these same repayment and ownership provisions. A secondary but also critical provision in formal lending and ownership contracts is the stipulation of the exact types of information which must be communicated to the investing financial institutions as well as the scheduling and frequency of presentation of this information.

The USA Securities and Exchange Commission ("SEC") drafts and implements detailed securities offering, trading, and financial disclosure regulations that act as a proxy for similar provisions in the formal contracts that financial institutions use and applies the regulations to publicly offered and traded debt and equity securities. The SEC also polices the compliance of these regulations for adequacy, quality and timeliness on behalf of investors in public securities. In so doing the SEC is acting as a surrogate for the contracts and compliance departments performing a like activity on behalf of private financial institutions. Researchers Bricker and Chandar have pointed out that the drafting and institution of the original Securities Laws in the early 1930's were at the least indirectly influenced by the Berle and Means studies of 1932.[28]

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26. Robert Bricker and Nandini Chandar, "Where Berle and Means went wrong: a reassessment of capital market agency and financial reporting", Accounting, Organizations and Society, 25 (2000), pp. 529-554 and Robert Straw, Simon Peck and Hans-Ueli Keller, EVA & The OECD Principles of Corporate Governance, Working Paper, p. 7.
27. OECD Principles of Corporate Governance, 1999, p. 2.
28. Robert Bricker and Nandini Chandar, 2000, p. 532.

A highly important objective of Corporate Governance principles is to preserve the rights of shareholders to their fair share of ownership from an economic basis as well as control basis concerning their investment. The divisionalization, instead of a "merger of equals" status for Chrysler, constitutes a subjugated role for control and influence over all investment and strategic decisions. Mr. Kerkorian and his sympathizers consider this status for Chrysler to be an expropriation of shareholder rights. In another recent study, the research team of LaPorta, Lopez-de-Salinas, Schleifer and Vishny theorized, "On average, investors recognize a risk of expropriation, penalizing firms that fail to contractually disclose information about themselves and to contractually bind themselves to treat investors well."[29] The method of recourse for investors can be, as is seen here for DaimlerChrysler, both market based in the devaluation of the company's shares and legally based in the filing of a class action investor lawsuit.

Also LaPorta et al.; referencing two separate studies in 2000 by Coffee and by Johnson, La Porta, Lopez-de-Salinas and Schleifer; clearly illustrated the distinctions between the history of the development of legal system in Germany versus that in the USA. An examination of these distinctions could provide clues to the background behind the behavior of Mr. Schrempp in the DailmlerChrysler situation. The civil law system of Germany, of which Mr. Schrempp would have most familiarity, relies almost exclusively on the black and white rules found directly in legislation and regulations. Judges in Germany employ little leeway in redressing a seemingly unfair situation, except as explicitly granted in the law. LaPorta et al. conclude,

> As a consequence, a corporate insider who finds a way not explicitly forbidden by the statutes to expropriate outside investors can proceed without fear of an adverse judicial ruling. Moreover, in civil law countries, courts do not intervene in self-dealing transactions as long as these have a plausible business purpose.[30]

The common law system of the USA, instead, relies on a collection of precedents set by earlier court rulings as well as a foundation of general principles including legislative intent and constitutional priority. When a dispute comes before a court, the judge is expected to rule based on application of precedent and principle, "such as fiduciary duty or fairness."[31] This judicial power provides a strong disincentive against expropriation of any type by insiders, ie. corporate executives, and, in turn, provides a strong position of enforcement for investors.

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29. LaPorta, Lopez-de-Salinas, Schleifer and Vishny, "Investor Protection and Governance", Journal of Financial Economics, January, 2000, Vol. 58 (1-2) pp. 3-27.
30. LaPorta, Lopez-de-Salinas, Schleifer and Vishny, 2000, p. 9.
31. LaPorta, Lopez-de-Salinas, Schleifer and Vishny, 2000, p. 9.

2.3. OECD Principle II. The Equitable Treatment of Shareholders

The concentration of shareholder voter power through blockholding of shares in public corporations translates directly into a concentration of control. Researchers Becht and Röell document the significant differences in concentration of voting power in European companies versus that found in American companies.[32] Table 1 following presents voter power concentration statistics for Germany and for the U.S., which Becht and Röell reference from earlier studies conducted by Becht and Böhmer for Germany and Becht for the U.S.

Table 1: Voter Power Concentration

Voting Power Stake Largest Range %	Germany (%)	Germany Cum(%)	USA (%)	USA Cum(%)
0-5	1.1	1.1	52.8	52.8
5-10	1.9	3.0	21.1	73.9
10-25	14.5	17.5	20.9	94.8
25-50	18.3	35.8	3.5	98.3
50-75	25.5	61.3	1.5	99.8
75-90	17.5	78.8	0.2	100
90-95	5.7	84.4	0	100
95-100	15.6	100	0	100

Notes: Voting Power Stake - is the range of the largest voting block for companies surveyed. (%) is the per cent of total companies in that country that fall in the respective range. Cum (%) is the cumulative per cent for the companies surveyed.

Source: Marco Becht and Ailsa Röell, 1999, p. 1053.

As can be seen from the table, the shareholder population of a majority of companies in Germany contain a single voting block with greater than 50% of the total voting power. In the USA, the majority falls in the 0-5% range. Immediately following the approval of the merger of Daimler-Benz and Chrysler, Deutsche Bank had a 12% shareholding interest and the Kuwait Emirate had 7%.[33] This means that prior to the merger, their ownership in

32. Marco Becht and Ailsa Röell, "Blockholdings in Europe: An international comparison", European Economic Review, 43 (1999), pp. 1049-1056.
33. Ralf P. Brammer, 2000, p. 261.

Daimler-Benz was approximately 20% and 10%, respectively. It can be inferred from the table that almost 9 out of every 10 publicly traded German firms contain a voting block of the size or greater than Deutsche Bank held in Daimler-Benz. In stark contrast, 9 out of every 10 American firms do not contain a voting block as large as 20%. Banks and other financial institutions play a major role in owner concentration in Germany.

Holman W. Jenkins, Jr., member of the editorial board of The Wall Street Journal critically advised, "[Mr. Schrempp] will have to stop hiding behind Deutsche Bank's big stake in the company and fully commit himself to listening to the stock market."[34] An editorial published in the English Edition of the Frankfurter Allgemeine illustratively entitled "Corporate Bonding", alternatively asserts that it was the severe problems that arose at Chrysler which forced Mr. Schrempp to abandon his intentions to "sincerely…forge a partnership" and was not the result of any premeditated deception. The editorial even goes so far as saying, "this assault by Mr. Kerkorian…is largely useless." However, the writer, Jürgen Dunsch, does not fully dismiss the lawsuit but concludes, "the U.S. lawsuit brings Mr Schempp and [major shareholder] Deutsche Bank even closer together. The danger is that the German-American divide within DaimlerChrysler will gradually become unbridgeable."[35]

LaPorta et al., referring to research by Allen and Gale, elaborated further on the differences between Germany and the USA affecting the equitable treatment of shareholders – that is the bank-centered versus market-centered configuration of their respective corporate governance systems. Executives in bank-centered systems are more influenced by the financial institutions and their relatively high concentration of equity in their firms (along with their lending oversight). Whereas, in the USA, where the Glass-Steagall regulations had historically not allowed traditional banks to make long-term equity investments in firms, a much higher dispersion of ownership has developed consisting of many individual and institutional investors.[36] Although LaPorta et al. discounted research by Edwards and Fischer and by Hellwig which suggests that corporate governance by German banks is ineffective, the existence of the influence of the two distinct governance systems is confirmed.[37] Bricker and Chandar also support this distinction between the German and American systems. They point out that Germany maintains a traditional ownership system concentrated in financial institutions with little influence held by individual investors, in direct contrast to the American system.[38] Finally, a study by Kaplan, as summarized in Table 2, also

34. Holman W. Jenkins, Jr., 2000, p. 8.
35. Jürgen Dunsch, "Corporate Bonding", Frankurter Allgemeine Zeitung, Europe Edition, No. 200/48, November 29, 2000, p. 1.
36. LaPorta, Lopez-de-Salinas, Schleifer and Vishny, 2000, p. 17.
37. LaPorta, Lopez-de-Salinas, Schleifer and Vishny, 2000, p. 18.

recognizes this distinction (see "Banking System" and "Ownership" categories) when comparing the German and USA corporate governance systems.[39]

Table 2: A Comparison of German and U.S. Governance Systems

	Germany	USA
BANKING SYSTEM	Universal Banking	Fragmented
OWNERSHIP	Concentrated: High Family/ Corporate/Bank	Diffuse/ Non-corporate
CAPITAL MARKETS	Relatively Illiquid	Very Liquid
TAKEOVER/CONTROL MARKET	Minor	Major

Source: Steven N. Kaplan, 1997, p. 87.

The "Capital Markets" category in Table 2 also draws attention to a potential dilemma in implementing cross-Atlantic investor relations systems. Becht explains that "Relatively Illiquid" markets in Germany stem to some extent from blockholding ownership. Even in many companies with measurably more liquid trading of shares, where there are fewer apparent ownership blocks, there exists various legal mechanisms which create controlling voting blocks. These instruments include bank proxy voting, share transfer restrictions, voting caps, multiple voting rights, and non-voting stock, among others. Such devices in turn are shown to have a negative impact on liquidity.

On the other end of the spectrum in the USA, "Very Liquid" securities markets are the rule. To explain this situation, Becht refers to a study by Coffee, which "argues that many institutional investors in the United States

38. Robert Bricker and Nandini Chandar, 2000, p. 543.
39. Steven N. Kaplan, "Corporate Governance and Corporate Performance: A Comparison of Germany, Japan, and the U.S.", Journal of Applied Corporate Finance, Vol. 9 No. 4, Winter 1997, pp. 86-93.

deliberately trade off control against liquidity."[40] This trade-off is also recognized by individual investors.[41] A highly plausible explanation is that American investors have a real and rational expectation that management will look after investors' interests. This confidence can result from the U.S. legal system, where regulation and enforcement have built up a clear record of shareholder protection, as compared to other legal systems in countries with less liquid trading in financial markets where shareholders' interests have historically not been a priority.

Either as an alternative or in addition to an investor protective legal system, U.S. shareholders may also believe in the concept of a general congruence of management and investor goals, stemming from a strongly consistent business culture and relatively well developed corporate governance system. Agency theory helps us to understand that when control is released, as occurs more readily in the U.S., investor expectations of direct accountablility of management are heightened. In a situation like DaimlerChrysler's, where control is entrusted (or turned over) to foreign management, it is reasonable to expect that investors will be closely monitoring management's behaviour to guard against incongruence of goals and the potential for expropriation.

2.4. OECD Principle III. The Role of Stakeholders in Corporate Governance

The OECD principles also recommend recognition of the roles performed by stakeholders and the interactions among them by specifically stating, "Corporate governance is affected by the relationships among participants in the governance system."[42] As was pointed out earlier, DaimlerChrysler is under fire from many stakeholders – investors, dealers, suppliers, employees, the press, etc. – not only for its operational and financial problems but also for its methods of communication. These stakeholders have made significant business and personal investments in developing their long-term oriented relationship with the firm. They would logically consider the firm's prior "merger of equals" oriented communications as an implicit contract forming a strategic basis for their continued cooperation with the firm. For all of these stakeholders, the losses incurred would be equal to the profit foregone, otherwise known as the "opportunity cost", through the implementation of a different strategy by DaimlerChrysler management than originally communicated. As we see from the DaimlerChrysler situation, U.S.

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40. Marco Becht, "European corporate governance: Trading off liquidity against control", European Economic Review, 43 (1999), pp. 1071-1083, p. 1072.
41. Marco Becht, 1999, p. 1080.
42. OECD Principles of Corporate Governance, 1999, p. 3.

stakeholders, particularly investors, are prepared to hold the leaders of foreign companies accountable through negative publicity in the media and through available legal means (ie. lawsuits) when these stakeholders have the impression that management's actions contradict their prior public statements of plans and intentions.

2.5. OECD Principle IV. Disclosure and Transparency

As Jenkins of The Wall Street Journal asserted in late 2000, "In the pinch…[Mr. Schrempp] has treated Mr. Kerkorian shabbily, avoiding meeting with him and disbanding the advisory board on which one of Mr. Kerkorian's aides sat", and Mr. Jenkins questions further, "Who can blame Mr. Kerkorian if he has concluded that the only way to get the man's attention is with a lawsuit?"[43] This behavior on the part of Mr. Schrempp is especially curious when a German study selecting DaimlerChrysler's invesor relations practice as a benchmark example for other firms observed that a key objective for the CEO's and CFO of DaimlerChrysler at the merger was to schedule direct contact at least once per year, if not more often, with each of the fifty largest investors in the company.[44] Therefore, it seems that where there was a clearly German national dominated executive leadership, there was also a predisposition to impose a dominant German investor relations culture. This could assist in explaining how Mr. Schrempp, despite his well documented respect for American business methods,[45] could have precipitated an error of omission in paying too little attention to individual minority investors, even one the size of Mr. Kerkorian.

Mr. Schrempp's time and energies were apparently directed primarily to his interactions with the Chrysler executives where he had placed his reliance and trust for integrating Daimler-Benz and Chrysler, as evidenced by his dual Stuttgart and Auburn Hills headquarters offices and "frequent flyer" mileage records between Stuttgart International and Detroit International airports. Certainly what also played a role in this specific situation was the entirely human psychological behavior of avoiding the discomfort and potential for conflict of working with a former rival. Mr. Kerkorian had launched a very unwelcome takeover battle for Chrysler in 1995 and was fended off by Mr. Eaton. Mr. Schrempp had already chosen sides and therefore depleted much of his personal "stock" of conciliation for Mr. Kerkorian in partnering with Mr. Eaton in sharing the chairman's office.

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43. Holman W. Jenkins, Jr., 2000, p . 8.
44. Ralf P. Brammer, 2000, p. 265.
45. Holman W. Jenkins, Jr., 2000, p . 8.

Unfortunately, a claim a lack of experience or understanding of disclosure and transparency requirements cannot entirely be used to excuse Mr. Schrempp or DaimlerChrysler in this situation. In fact, Daimler-Benz was the first major German company to list its shares on the New York Stock Exchange when it did so in 1993, subjecting the company to all the pertinant U.S. securities regulations. There also appears to be much room for improvement in the investor relations practices of German firms in general, when dealing with the U.S. public. A recent study conducted by the German-American Chamber of Commerce office in New York describes these firms as arrogant, inflexible, and lacking in transparence.[46] This same difficulty in managing investor relations practices encountered by a leader in German-American financing strategy, should serve as a warning to far less experienced firms.

In this situation, DaimlerChrysler can still succeed in its defense by establishing that a "merger of equals" was the original intent of Mr. Schrempp and other Daimler-Benz representatives, even though Chrysler has now been divisionalized. As long as it can be demonstrated that the divisionalization resulted from decisions made after the merger from performance factors and reasonable business requirements which also developed subsequent to the merger, the safe harbor is invoked. The specific definition of one type of forward-looking statement in the Private Securities Litigation Reform Act of 1995 that would be protected in this situation is "a statement of the plans and objectives of management for future operations, including plans or objectives relating to the products or services of the issuer ".[47]

2.6. OECD Principle V. The Responsibilities of the Board

Corporation law in Germany calls for a system of "codetermination" in large public companies with a unique dual board structure - a supervisory board and a management board. The supervisory board, like the board of directors in other countries, appoints top executive management. But unlike most mixed boards, none of these executives can sit on the supervisory board. The supervisory board contains at least one third and up to one half of its members elected by employees. Shareholders elect the other members and have the additional right to elect the chairman. This structure may appear to set limitations on Mr. Schrempp, as he is chairman of the management board, but not of the supervisory board. However, the codetermination system often empowers management or a single dominant shareholder and reduces

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46. Martin Halusa, „Deutsche Werben an der Wall Street", Die Welt, October 12, 2000, p. 16.
47. Bruce W. Marcus and Sherwood Lee Wallace, New Dimensions in Investor Relations: competing for capital in the 21st century, John Wiley & Sons, Inc., New York, 1997, p. 257.

incidence of unfriendly takeovers[48], as also noted in the last row of table 2, where the influence is described as "minor" in Germany as compared to "major" in the U.S.. Sir Adrian Cadbury interestingly asserted a few years after the merger, that the Chrysler board of directors with Mr. Eaton as Chairman had input to the merger negotiations as early as February, 1998. Mr Schrempp, on the other hand, is said to have not informed his management board until early April, and his supervisory board was only notified one day before the public merger announcement in May.[49]

In the Financial Times interview that was the source of all of the difficulty for Mr. Schrempp, he made another significant statement that was not nearly as often quoted:

> 'The stock performance over the last 12 months was lousy, and I have a short-term problem in telling the story,' he admits. 'But I don't need outside pressure. The pressure I put on myself is more than could be put on anybody.'[50]

On one hand, perhaps Mr. Scrempp is his own toughest critic, and it is quite reasonable to assume from his numerous accomplishments that he is highly self-motivated. On the other hand, some followers of the situation may agree with the German bank analyst who said, "'Mr. Schrempp has talked himself into a very tight corner. He has been incredibly arrogant in disregarding the shareholders' interests'."[51] The OECD principles hold the board of directors responsible ultimately for "overseeing the process of disclosure and communications."[52] The directors can only fulfill this responsibility successfully when the chief executive officer, Mr. Schrempp, is willing to subjugate himself and accept accountability to the board.

The Corporate Governance Principles and various research studies and experts referenced in this study have shown, a chief executive like Mr. Schrempp is far better off if he ensures that he keeps an open line of

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48. Michael J. Rubach and Terrence C. Sebora, "Comparative Corporate Governance: Competitive Implications of an Emerging Convergence", Journal of World Business, 33(2), 1998, pp. 167-184, p. 176.
    Stephen M. Bainbridge, "Participatory Management Within a Theory of the Firm", The Journal of Corporation Law, Vol 21 No 4, Summer 1996, pp. 657-730, Footnote 181, p. 689.
    Hartmut Wächter and Theo Stengelhofen, "Human Resource Management in a Unified Germany", Employee Relations, Vol 14 No 4, 1992, 21-37, p. 22.
49. N.N., "The way we govern now", The Economist, www.economist.com, January 9, 2003, pp. 2-3 as found in Adrian Cadbury, "Corporate Governance and Chairmanship: a Personal View", Oxford University Press, 2002.
50. Tim Burt & Richard Lambert, 2000.
51. Susanne Preuß, "Deutsche Bank Closes Ranks With Schrempp As DaimlerChrysler Boss Comes Under Fire", Frankfurter Allgemeine Zeitung, English Edition, November 29, 2000, No. 200/48, p. 1.
52. OECD Principles of Corporate Governance, 1999, p. 9.

communication with his investors and other important stakeholders. It is important that he actively listens to their opinions, gives a full account to their recommendations, and communicates regularly how the company's strategies and operations are protecting and fulfilling their interests. Perhaps recognizing his own responsibility as chairman of the management board, or under advice of supervisory board members, through a swift and apparently sincere apology for his Financial Times statements, Mr. Schrempp has done what he can to calm the critics and rebuild vital credibilitiy in the financial markets and stakeholder interest groups.

3. Conclusion

Recent studies comparing German and U.S. corporate governance practices coupled with statements and events surrounding the DaimlerChrysler crisis, do highlight major differences in the two systems, particularly the imbalance of influence in German corporations from banks and blockholding shareholders. However, the recent passage of the KonTraG in Germany demonstrates a significant step to move German business closer towards a corporate governance system such as that outlined in the OECD principles. It will take a concerted effort on the part of members of German boards and management to understand, recognize and overcome the historically based governance structures and habits which hamper compliance with these new principles, especially regarding investor and stakeholder relations and communication.

For Mr. Schrempp and DaimlerChrysler more specifically, even if there proves to be no merit to Mr. Kerkorian's lawsuit from a regulatory or legal standpoint, non-fulfillment of stakeholders' reasonable expectations may have erected walls between the Chrysler and Daimler-Benz groups. Communications issues originating on both sides of the Atlantic in the combined company have had negative repercussions and caused or worsened the severe hardships placed on a large population of stakeholders and shareholders, primarily those with direct or indirect interests in the Chrysler business unit. This particular situation could also have a chilling effect on boards of German and other European corporations considering U.S. cross border investments and public offerings.

It is critical from a strategic viewpoint to reject the train of thought which has unfortunately been transmitted by the media that the German and U.S. business cultures are incompatible. Hopefully further undue harm to the relations of these two important economic partners can be avoided. Especially in light of the major failings in corporate governance in both the USA and Germany over recent years, neither system can be held up as a pristine example in today's environment, making it all the more critical to understand and update corporate governance principles and implement appropriate reforms.