

Battle of the systems or multi-level game?

Domestic sources of Anglo-German quarrels over EU takeover law and worker consultation

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Abstract: Why have British and German spent the past thirty years in disagreement over European Commission proposals to harmonize legislation concerning worker consultation and company takeovers? This paper shows that functionalist "battle of the systems" explanations are unsatisfactory because they neglect the political dimension of institutional design. Instead of relative preference homogeneity within countries based on a joint and stable vision of a common good, government positions reflect the result of struggles at the domestic level between and within competing groups. Moreover, different political dynamics are at work in the two policy areas. British and German employer federations united in opposition against the EU-wide spread of "German-style" worker consultation, while unions in both countries were in favour. On the takeover directive, the German employer federations have joined forces with German unions to lobby against the spread of "British style" takeover rules, while the CBI has aligned with financial sector interests in order to promote it. After presenting empirical evidence, I discuss its implications for theories on institutional complementarity, path dependence and two-level games. The paper ends with some thoughts on why German and British employer federations joined forces against extensive worker consultation, but not against easy takeovers.

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For decades, German and British governments in the Council of Ministers have resisted legal harmonization efforts that threatened to change to their national arrangements concerning worker consultation and hostile takeovers. What explains this resistance?

The Varieties of Capitalism literature identifies good reasons why Britain and Germany *ought* to resist harmonization in the areas of worker consultation and takeover law. Takeover rules, both directly and through their effect on stock market development, and rules pertaining to worker consultation are portrayed as vital components of the institutional infrastructures generating the respective comparative institutional advantages of liberal and organized market economies.ⁱ

For those who draw a distinction between ought and is, the Varieties of Capitalism literature still lacks a satisfactory explanation for why the British and German governments actually *do* resist harmonization. Hall and Soskice (2001) deal with the latter question only in passing. They sketch a functionalist answer, arguing that the effect of institutions – comparative institutional advantage in certain areas – also provides the key to understanding why they are sustained. In their own words, governments' "stance towards new regulatory initiatives will be influenced by judgments about whether those initiatives are likely to sustain or undermine the comparative institutional advantages of their nation's economy. Governments should be inclined to support such initiatives only when they do not threaten the institutions most crucial to the competitive advantages their firms enjoy." (see also Fioretos 1998; Fioretos 2001; Hall and Soskice 2001: 52).

The functionalist explanation is unsatisfactory because it neglects the political dimension of institutional design. Even if the arrangements concerning worker codetermination and takeovers are indeed vital components of the British and German production regimes it remains to be explained why democratically elected governments act to preserve them. The domestic political dimension of the institutional choice problem could be ignored if it were true that "interest groups and

governments largely share a commitment to maximizing the comparative institutional advantages of their respective market economy." (Fioretos 2001: 225), but this assumption is too questionable (because of externalities, collective action problems, incomplete information etc.) to be accepted without empirical proof.

Recent analytical work on the sources of path dependency (e.g. Mahoney 2000; Pierson 2000; Thelen 2000) has emphasized non-functionalist alternative reasons why institutions persist over time. Power-distributional approaches highlight the fact that institutional arrangements give rise to and are in turn sustained by asymmetries of power and might therefore persist regardless of whether they are optimal from the vantage point of society as a whole (e.g. Knight 1992). Cultural-sociological explanations emphasize limits of rationality, arguing that institutions may not be the product of means-ends-calculations but might instead persist simply because they are not being called into question, or because of their significance within a broader cultural context (e.g. DiMaggio and Powell 1991; Dobbin 1994) (March and Olsen 1989).

My research aims to provide an empirical basis for assessing these competing explanations for persistent institutional divergence in the areas of worker consultation and takeover law. It does so by focusing on the domestic political dynamics underlying government positions in negotiations over legal harmonization. Can intergovernmental disagreement on corporate governance issues be characterized as a battle between different economic systems, with interests at the domestic level more or less homogenous and relatively uncontested? Or is the international level just one part of a multilevel game, with intense struggles over the shape of institutions also taking place domestically, and divergent governmental preferences not so much the result of differences in the structure of countries' economic institutional environment, but more due to differences in their political arenas?

My empirical findings to date suggest that different political dynamics are at work in the two policy areas. I have not yet completed my field research, but from qualitative data gathered so far, two preliminary observations have emerged:

First, the institutional preferences of national employer federations diverge much more sharply on the takeover question than on worker consultation issues. Despite their different domestic institutional environments, German and British employers have fought side by side against EU-wide imposition of mandatory worker

consultation. On the issue of takeover liberalisation, they have pulled in opposite directions.

Second, all other relevant groups besides employer federations have broadly similar preferences across countries for both policy areas, but on the takeover issues, there is greater cross-country variation concerning the degree of mobilisation and/or "voice" of comparable groups i.e. City representatives played a far more prominent part in debates over the takeover directive than their German counterparts, while the reverse holds true for unions.

In other words, the debate over worker consultation is subject to centrifugal political tensions within countries, with workers and owners pulling in opposite directions, while the domestic cleavage structure on the takeover issue at first glance seems to approximate a "battle of the systems" situation characterized by relative homogeneity of institutional preferences among relevant groups within countries. However, the latter impression is partly due to the fact that different groups are relevant in each country.

After presenting empirical evidence for the above claim, I will discuss its implications for theories on institutional complementarity, path dependence and two-level games. The paper ends with some thoughts on why German and British employer federations joined forces against extensive worker consultation, but not against easy takeovers.

2.1 Worker consultation rules

Disagreement among EU member states over the form and extent of worker consultation rights has been a prime cause of harmonization failure in the areas of European company law and labor law for more than thirty years, stretching over numerous draft directives and several issue areas. The question of *worker representation at the board level* has contributed to the rejection of the Fifth company law directive on the internal organization and structure of public liability companies (1972, 1983 drafts), the tenth company law directive on cross-border mergers (1985 draft) and several versions of the European Company Statute (1970, 1975, 1989, 1991). *Information and consultation rights of employees through works councils* were a sticking point of negotiations over early versions of the European Company Statute (1970, 1975 drafts), the so-called "Vredeling directive" (1981, 1983 drafts), the European Works Councils directive (1994), and the Information and Consultation

directive (2001). (The latter two did pass, but under qualified majority voting and, in the case of the European Works Council directive, without British participation¹.)

Government positions diverged on just about every conceivable question in this domain: How much, if any, representation should employees have at the board level? Should bodies of employee representation below board level be composed of workers only, or should they include management? Should the choice of employee representatives on works council and board proceed through election by all employees or through appointment by trade unions represented in the company? Was employee representation above the level of the individual establishment desirable or not? Should the participation rights of employees be limited to information or should they also encompass participation or even codetermination? What types of information should employees be entitled to, etc..

German and British governments frequently found themselves on opposite sides in these negotiations, each seeking to defend its own domestic arrangements. The social-liberal German government of the 1970s demanded that the dual board structure and employee representation on the supervisory board characteristic of German corporate governance serve as the model for the fifth directive. (Streeck 1997:647) Helmut Kohl's center-right government during the 1980s insisted on limiting the workforce of "European Economic Interest Groupings" to 500 employees to avoid complications with existing German co-determination legislation (Kolvenbach 1990: 763) and demanded additional safeguards for German codetermination rights in the context of the 10th directive on cross-border mergers (Kolvenbach 1990: 742) and on the European company statute. (Dawkins 1988) During the 1990s, the CDU-FDP coalition strongly promoted the European Works Council directive (Bassett 1994) and threatened to reject it if it were watered down too far. (Goodhart 1991)

By contrast, Britain under Thatcher categorically rejected all proposals for "non-voluntary" consultation arrangements. (see e.g. Dawkins 1988; DTI 1983; Todd 1988; Wyles 1982) Under Major, opposition to the European Works Council Directive was one of the reasons why Britain chose to opt-out from the Social Chapter of the Maastricht Treaty. Blair's Labour government did sign up to the European Works Council directive and to the Information and Consultation directive, but not without

¹ The British Conservative government under John Major had secured an opt-out from the Social Chapter of the Maastricht Treaty. Tony Blair's Labour government signed up to the to the European Works Councils directive after coming into power in 1997.

lobbying hard to water down the rules. (Europolitique 2000; Inman 2002; Trades Union Congress (TUC) 2001)^{2 3}

These regime-defensive attitudes in themselves are not surprising. Had governments wanted to dismantle their respective institutional arrangements, they could have done so at the national level - unless they had reason to fear more resistance at home than via the EU. In fact, government attitudes toward EU decisions are broadly mirrored by political choices at home. The German codetermination law, passed in 1976 under Brandt's social-liberal administration, was been left untouched throughout the Kohl era. In the UK, enthusiastic embracement of EU efforts to expand worker rights would have been more than strange, given Thatcher's aggressive trade union policies (Mitchell 1987) and Blair's reluctance to re-establish ties with organised labor. (Howell 2000)

The interesting question is thus not why the British and German governments at EU level defended the regimes which they had shaped domestically, but to compare the underlying constellations of interest in the two countries that empowered their governments to make different institutional choices both at home and internationally. Doing so leads to a rejection of the functionalist battle of the systems hypothesis. It is clearly not the case that "interest groups and governments largely share a commitment to maximizing the comparative institutional advantages of their respective market economy."⁴

Even within governments, decisions pertaining to core elements of the respective production regimes were at times subject to political strife. With regard to EU measures, this was the case during the Kohl administration between labor minister Norbert Blüm (CDU) and justice minister Hans Engelhard (FDP). (Engelhard 1988; Handelsblatt 1986) Reform of the German codetermination law was the subject of internal struggle during Brandt's social-liberal coalition government of the 1970s between economics minister Hans Friedrichs (FDP) and labor minister Walter Arendt

² In the case of the Works Councils Directive, it had also become evident that the opt-out was not worth much, because British multinationals still had to provide European Works Councils for their employees on the continent. The opt-out deprived them of participating in shaping the rules by which they were bound.

³ BUT note that albeit watered down, elements considered "alien" to a liberal production regime have been introduced. It is too early to evaluate their effect, but it shows that production regimes are not cast in stone.

⁴ Fioretos, Karl-Orfeo. 2001. The Domestic Sources of Multilateral Preferences: Varieties of Capitalism in the European Community. In *Varieties of Capitalism*, edited by P. Hall and D. Soskice. Oxford: Oxford University Press.

(SPD), (Wirtschaftswoche 1976) and under Schröder between economics minister Werner Müller (SPD) and labor minister Walter Riester (SPD). (Reiermann, Sauga, and Schäfer 2001; Sauga and Schallenberg 2001; Spiegel 2000c; Spiegel 2000d; Spiegel 2001)

Intense contestation of production regimes from within is even more visible at the level of domestic groups. German employer federations throughout the period have lobbied alongside their British counterparts *against* consultation requirements, while British unions like their German peers have sought their expansion.

Regarding German employer attitudes toward EU initiatives pertaining to worker consultation, four points are noteworthy. First, peak federations throughout the period have strongly objected to all consultation requirements that would go beyond what they already had at the national level. Among other things, the BDA opposed catalogization of issues that require supervisory board consent, (BDA 1982: 218) lowering the threshold for worker representation on the board level from 2000 to 1000 employees, (BDA 1982: 218; BDA and BDI 1983b: 7) extending the scope of information rights granted to employees (BDA and BDI 1983a: 5) and adding European Works Councils to national arrangements. (BDA and BDI 1991: 3)

Second, during the 1980s and early 1990s, the prevailing mood within the BDA seems to have been that German employers had nothing to gain and much to lose from European debates over worker consultation. One reason for this attitude was a strong fear that European initiatives would rekindle the codetermination disputes at the national level, forcing them to make more concessions to strong German unions. (BDA and BDI 1983a: 4; BDA and BDI 1989: 3) Another concern was that European measures would cause “structure destroying changes to the Works Constitution Act”(BDA and BDI 1983a: 3). With regard to the Vredeling proposal, the BDA complained about the lack of "major basic principles of the German Works Constitution Act, which are decisive and essential for its function and its total positive evaluation", including the legal obligation for trustworthy co-operation, the "precept of neutrality", which obliges German works councils to refrain from political and trade union activity, and the strike prohibition for employee representatives. (BDA and BDI 1983a: 6f; BDA and BDI 1991: 3)

Third, the German employer federations made it clear that they did not want to see the export of German-style worker consultation rules to the rest of Europe. (BDA and BDI 1981: 2; BDA and BDI 1983b: 2) This attitude stems partly from concerns

that German multinationals would be forced to deal more with foreign worker representatives, be it through European Works Councils or through the election of foreign worker representatives onto supervisory boards. Fears of "foreign union members who are not familiar with our national practices" (Gesamtmetall 1970) and especially of "communist trade unions, political party bound and obligated to the ideology of class war according to their programmatic understanding" (BDA and BDI 1983a: 7f) are a recurrent theme in employer statements concerning EU legislative proposals (see also BDA and BDI 1983b: 9; BDA and BDI 1991: 8, 13; Parkes 1991) There were also concerns that any concessions on worker consultation would strengthen the international union movement, leading to further demands, not only within the EEC (Gesamtmetall 1970) but also in the UN and OECD. (BDA and BDI 1981: 3) Beyond that, the BDA also claimed to be concerned about the competitiveness the European market as a whole. (BDA and BDI 1983b: 6)

Fourth, German employers repeatedly stressed the need for harmonization onto a low-consultation model in order to preserve the attractiveness of Germany as a location for foreign investment and of German companies as partners in cross-border mergers. (afd-Nachrichtenagentur 2000; BDA 2000; BDA and BDI 1985: 5; BDA and BDI 1989: 53; BDA et al. 1998; Zeit 2001)

The contrast between employer preferences and government action on worker consultation is also reflected in lobbying activity regarding domestic legislation. During the 1970s, the German employer federations fought a bitter campaign to prevent the passage of the 1976 codetermination law, arguing that parity representation on the supervisory board would lead to trade union control of the economy and loss of business efficiency. (see e.g. EIRR 1974; Thüsing 1976) After its passage, they challenged it in the German constitutional court. (see e.g. Sieling-Wendeling 1978) After losing in court, the peak employer federation BDA issued advice to its members on how to minimize the impact of the law by limiting the formal powers of the supervisory board. (Wirtschaftswoche 1979) Twenty years later, complaints about the system have not subsided. Hans-Olaf Henkel, head of the German industry peak association BDI during the late 1990s, and his successor Rogowski have lead fierce attacks against worker representation on the supervisory board. (see Handelsblatt 2003a; Henkel 1998) In the same vein, albeit less radical in tone, Hilmar Kopper, president of the supervisory board of Daimler-Chrysler stated in a 2001 interview with Die Zeit that that, from a managerial point of view, the German

system of worker representation on the supervisory board was anachronistic and detrimental to good corporate governance. (Zeit 2001)

While supervisory board representation seems to have been the strongest source of employer misgivings, the system of worker representation on the shopfloor via works councils has also come under attack. In a three-page position paper, the BDA in 2001 demanded reductions in the scope of codetermination rights, in the size of works councils and the number of full-time worker representatives, and an increase in the number of medium-size firms that are exempt from codetermination requirements. The BDA further demanded legal recourse for companies to sue their works councils if the latter acted “contrary to their duties”. It also proposed the introduction of a preliminary poll preceding works councils elections, where a majority of employees would have to pronounce in favor of having a works council at all. (Spiegel 2000b)

This is not to say that the lobbying campaigns of the peak federations have always met with unanimous approval from all German employers. Relations between the peak employer federation BDA and the peak industry federation BDI have at times been strained because the BDA took a more moderate approach to questions concerning labor relations (see e.g. Spiegel 1996; Spiegel 2000a) The confrontational rhetoric of BDI president Henkel also earned criticism from managers of large companies, including Jürgen Schrempp of Daimler-Benz, Lothar Späth of Jenoptik (previous CDU Minister president of Baden-Württemberg), Veba director Ulrich Hartmann, and Siemens boss Heinrich von Pierer. Even Manfred Schneider, CEO of Bayer and "not known as a soft-liner", distanced himself of Henkel's loud criticism. The German Association of Industry and Commerce (Deutscher Industrie- und Handelstag, DIHT) reported a flood of complaint letters regarding Henkel's rhetoric from the managers of medium-sized enterprises. (see also Spiegel 1998a; cf. Spiegel 1998b) Likewise, Rogowski's recent attack on codetermination received only a cautious welcome from the BDA and was rejected openly by some employers. (Handelsblatt 2003b)

Nevertheless, despite these disputes within the employer camp regarding the pace and manner in which existing rules should be rolled back, I do not know of a single instance in which an employer has favoured the extension of mandatory worker consultation. It therefore seems safe to say that it was not German employers who pushed their government to defend the consultation aspect of the German production

regime. Cross-country differences in the positions of peak employer associations are at best a matter of degree, not of fundamental direction. Neither British nor German employers favored the spread of consultation requirements.

Within the union camp, the reverse holds true. British unions, like their German counterparts, have always demanded legislation that would be regarded alien to a "liberal production regime", although it needs to be stressed that, until the mid-1980s, differences in strategic and ideological orientation prevented unions in the two countries from developing a joint vision regarding the form of increased worker consultation. Strategically, the TUC in the early period of negotiations had fixed its mind on maintaining a "single channel of representation". Ideologically, it did not want unions to share responsibility in company decision-making.

With regard to board level representation, this meant that the TUC, like the DGB, favoured parity representation of workers on the company board, (TUC 1974) but unlike its German counterparts, it wanted representatives to be accountable only to their fellow workers, without having to take responsibility for company performance (Gundelach 1976: 38; Nagels and Sorge 1977: 154). Furthermore, to maintain the "single channel of representation", British representatives were to be elected through the trade union machinery i.e. stewards' committees rather than through the workforce as a whole. (Lloyd 1983; Nagels and Sorge 1977: 154)

With regard to consultation through works councils, the TUC position during the 1970s was ambivalent. At the national level, it rejected them as a "second channel of representation" which would undermine the strength of the union movement. (Gundelach 1976: 35) At the European level i.e. as European Works Councils in the context of the European Company Statute, it reluctantly accepted them as a means of international union cooperation. Like board representatives, British EWC members were to be elected through trade union machinery. (Nagels and Sorge 1977: 154)

From the 1980s onwards, cross-country differences in union attitudes grew weaker as TUC skepticism was replaced by enthusiasm for European legislative initiatives. In 1982, David Lea, assistant general secretary of the British TUC and chairman of the ETUC committee on labor law, declared that "it is nonsense to set up something like the Common Market and to aim at industrial change on a European scale without giving the unions some opportunity of getting together themselves." (Wyles and Lorenz 1982) In 1983, the TUC endorsed the Vredeling proposal on the

grounds that "voluntary exhortation" for increased consultation and information was futile, and that "the best way to ensure that best practice is followed is to systematize and codify it, which is precisely the point of the draft directive". (Lloyd 1983) The main TUC criticisms concerning the Vredeling directive were that the 1000 employee threshold determining application of the directive was too high and that the requirement to provide information at least annually was significantly less useful than the six monthly frequency of the original proposal. (EIRR 1984)

In 1991 the TUC congress adopted a motion calling for an examination of "how features of the Franco-German approach to industrial relations, such as works councils and greater rights to information and consultation, might be adapted to British circumstances". Trade union leaders called for a system whereby, in the words of one speaker: "Rights are underwritten by law, representation is guaranteed in every workplace, employers are obliged to discuss a wider agenda with their staff." (EIRR 1994) By the mid-1990s, the TUC had become an enthusiastic supporter of European Works Council legislation. (EIRR 1994) The traditional hostility of the British left toward the European Community had disappeared to such a degree that John Edmonds, general secretary of the GMB union, could in 1994 declare that "For the Conservatives, Europe means internal warfare", but for unions it means raising standards at work and prosperity." (Bassett 1994)

This change of heart was partly due to Thatcher's aggressive anti-union policies and dramatic falls in membership and bargaining coverage. In the words of a 1994 paper commissioned by the TUC, "the organizational problems faced by British trade unions over the 1980s have prompted renewed debate about the relevance of Continental experience of employee participation structures for industrial democracy." (EIRR 1994)

In sum, British and German governmental preferences on worker consultation do not reflect a mere clash of fundamentally incompatible economic systems that are universally cherished at home. Instead, throughout the period of negotiations, there were intense struggles within countries over legislative efforts in this area.

2. Takeover legislation

European Commission attempts to harmonize rules governing company takeovers stretch back to the early 1970s, but to date, no agreement has been reached. A 1974 report on "Takeover offers and other offers" (Comm. Doc. XI/56/74), like

later drafts, was strongly influenced by the UK City Code. Due to limited interest in the member states, the project was abandoned after several years of discussion. (cf. Berglöf and Burkart 2003: 189) (*I am still searching for details on the content of these discussions.*) The drive towards completion of the internal market, coupled with a number of large scale controversial takeover battles, brought the issue back onto the agenda in the late 1980s. A draft directive presented in 1989 was dropped after three years of negotiation among member states. A new draft was presented in February 1997. By June 1999 the Internal Market Council had reached political agreement except for continuing disagreement between the UK and Spain over the question of the appropriate supervisory authority for take-over bids in Gibraltar. (Commission 1999) A year later, this issue was resolved and the Council in June 2000 adopted a common position on the directive. In December, the European Parliament, mobilized by its German Christian Democrat rapporteur, voiced major objections to the Council proposal. In April 2001, the German government withdrew its support from the common position. A conciliation procedure was launched, but on July 4, the compromise text was rejected in the European Parliament by the narrowest possible margin of one vote. In view of the continued political tensions surrounding the directive, the Commission decided to postpone presentation of a new draft, originally planned for July 2002, until after the September elections in Germany. (Guerrera 2002; Handelsblatt 2002) The latest draft, presented in October 2002, is still under negotiation.

The general aims of the directive are to facilitate cross-border company bids, protect minority shareholders and encourage corporate restructuring. The exact content of the directive and subjects of discussion have varied over time. During the early 1990s, a main sticking point was the desirability of a mandatory bid rule⁵. Later on, debate shifted onto the neutrality rule⁶ and the break-through rule⁷. Employee

⁵ Under a mandatory bid rule, a buyer trying to acquire control of a firm would have to bid for *all* outstanding shares at the *same* “equitable” price. Its purpose is to protect minority shareholders against coercive bidding practices.

⁶ Under the neutrality rule (article 9 of the current draft directive), the board of a company subject to a bid has to call a general shareholder meeting to obtain authorization for any action other than seeking alternative offers that could lead to the frustration of the bid. Under this rule, managers of a target company are banned from raising new capital, making significant acquisitions or selling significant assets unless they obtain explicit shareholder approval.

⁷ The breakthrough rule (article 11 of the current draft directive), empowers a bidder to override measures deviating from the one-share-one-vote principle once he has acquired 75 per cent of

consultation rights during takeover bids, disclosure requirements, the acceptability of non-cash offers and the relevant place of jurisdiction were also controversial.

British governments from the onset of negotiations have pushed for measures that would spread their own liberal takeover regime to the rest of Europe. (see e.g. Jonquières and Rice 1990; Rodgers 1989) They opposed those aspects of the directive that threatened to make takeovers more difficult in the UK. In particular, they feared that a switch from their traditional non-statutory system to a system of regulation through the courts would increase tactical litigation and thereby delay the conclusion of deals (see e.g. Armstrong 1999; Dobie 1991a; Financial Times 1991; Rice 1991b) Since January 2003, the British government has backed Germany's position on the takeover directive, reportedly to obtain German support for British efforts to water down the directive on Temporary Agency Workers⁸. (see European Report 2003; Guerrera and Jennen 2003) According to the joint British-German stance, the directive is not acceptable unless it ensures a complete "level playing field" by outlawing even more defensive measures than envisaged in the original proposal. At first glance this seems entirely in line with British calls for liberalization. Nevertheless, it does represent a sacrifice for Britain because it is likely to result in no directive at all. However, the British change of attitude does not represent a departure from the ideal of a liberal takeover regime across Europe, but merely the realization that the directive in its present form will not bring it about and is therefore "not worth the paper it is written on".

The German position is more difficult to capture, because it displays some inconsistencies over time and across issues⁹. Nevertheless, it seems fair to say that, for most of the period, German governments have resisted the adoption of British-style takeover rules. During the early 1990s, neither Bundestag nor Bundesrat saw any need for EU regulation in the area of takeovers. (Deutscher Bundesrat 1989; Deutscher Bundestag 1990) In EU negotiations at the time, the Kohl's center-right government among other things strongly opposed the neutrality rule, which would

shares in the target company. The measures concerned include voting caps, dual class shares, dual or multiple voting rights and restrictions on the transfer of securities.

⁸ The aim of this directive is to give temporary workers and long-term staff identical rights to pay and conditions.

⁹For example, the German government and the BDI long opposed the mandatory bid rule, which, while protecting shareholders, renders takeovers more difficult. The British government and the CBI were in favour. The reasons are too complex to be dealt with here and are relegated to a separate working paper that will be forthcoming shortly.

force the board of a target company seek shareholder approval before using poison pills. (Europolitique 1991; Europolitique 1992); (see also Deutscher Bundesrat 1989). After taking power in 1998, Schröder's center-left government initially lent its support to the takeover directive, which seemed to complement corporate governance reforms at the domestic level [see Cioffi, 2002 #2610; (Höpner 2003). However, shortly after the Mannesmann takeover, and only weeks before the final vote in the European Parliament, the German government in April 2001 withdrew from the common position which had been adopted by the Council of Ministers the year before. Three weeks later, all German MEPs voted against the directive. The official German complaint was that the directive would leave German companies "asymmetrically vulnerable" because multiple voting rights, which are already illegal in Germany but not in France and Scandinavia, are left untouched by the directive. Since then, German politicians have demanded that a takeover directive should either rule out all defence mechanisms or none. There is widespread suspicion that it would prefer the latter, and some believe that the German call for a complete level playing field was uttered in the full intent of provoking such widespread protest from other member states that it would cause the directive to fold altogether.

German and British industry associations have pulled in opposite directions on the takeover directive, unlike in the worker consultation case, where they have fought side by side. During the early 1990s, the German federations (BDA and BDI), like the German government, questioned the need for any EU-wide regulation (BDA 1989: 159) and opposed the radical dismantling of takeover barriers, including multiple voting rights. (BDA 1992: 15) (In 1998, multiple voting rights were abolished in Germany. Since then, German employer federations like the German government have called for their abolition across the European Union.) The German employer federations also opposed the neutrality rule on the grounds that there would rarely be enough time during bids to call a shareholder assembly (BDA and BDI 1998). This view is echoed in statements from prominent individual CEOs, including Wendelin Wiedeking, the executive board chairman of Porsche. (Wiedeking 2001) Executives of Volkswagen and chemical giant BASF were reportedly among those leading the lobbying campaign against the directive in the spring of 2001. (Dombey and Williamson 2001)

By contrast, British companies in the early 1990s exercised pressure on their government to push for a harmonization of takeover rules across the European Union. Their complaint was that, while they could not easily make contested bids in Europe, continental firms had the freedom to buy what they wanted in the UK, leaving British industry at a disadvantage in a single European market. (cf. Rodgers 1989) In 2000, Rod Armitage, head of legal affairs at the CBI, complained that amendments to the directive that would grant management powers to use defensive measures would reduce investor-protection and create asymmetries, as defensive actions permitted by member state regulatory authorities would inevitably differ. (Castle 2000) More striking than the call for a level playing field -which in principle could be satisfied either by exporting the British liberal regime or building up defences at home- is the unambiguous support of the Confederation of British Industry for a liberal takeover regime. In its written evidence to the Commons trade and industry committee inquiry on takeovers and mergers, the CBI said that it had 'serious problems' with the draft directive because it would threaten "the whole basis of the UK's efficient and flexible approach to the takeover process and mergers", and that any attempts to make the system more rigid so as to make takeovers more difficult would be strongly opposed by UK business (cf. Rice 1991a).

In neither country was there unanimity among industrial employers. Karl-Hermann Baumann, chair of the supervisory board of Siemens, the German electronics company, said the defeat of the directive would "send the wrong signal". (Dombey and Williamson 2001) A representative of British American Tobacco (BAT) expressed his dissatisfaction with the British takeover system to a House of Commons committee on the directive, arguing that the Takeover Panel was unaccountable and had unfair procedures, that there was secrecy and lack of certainty about the way it operated, that the draft takeover directive would cure those defects and present an opportunity to enhance the quality of the regulation of takeovers in the UK, and that a new body properly constituted and properly accountable to parliament should be set up to be the UK supervisory body under the European proposals. (cf. Rice 1991a)

However, judging from the information I have gathered to date, such dissenters within the national employer federations are in a clear minority in both countries. Broadly speaking, employer federations in each country fought to maintain the system they were embedded in. with German companies wanted to keep their

protections, while the British never sought to obtain them and opted instead for trying to spread their own liberal system to the rest of Europe.

Comparable cross-country differences do not exist among any of the other groups mobilized on the takeover directive. Unions in both countries have expressed their aversion to a liberal takeover regime. The DGB commented in the context of debate over the German takeover law that “shareholder value orientation is associated with negative labor market consequences, such as cost reduction through rationalization and job reduction through outsourcing.” (DGB 2000) In the same vein, the secretary general of the British Mining, Science Finance Union (MSF) observed that “[t]he UK's voluntary code leads to more takeovers and mergers in the UK than the rest of the EU. There is no evidence that all of these mergers benefit the consumers, shareholders, employees or society in the long term. However, they do earn the takeover consultancy industry a considerable and growing amount of income - at whose expense?” (Lyons 1997) To insure adequate consideration of employee interests, German and British unions have called for better information and consultation in the context of takeover bids. (DGB 2000; Lyons 2001; TUC 2001)¹⁰German unions also campaigned heavily against the neutrality rule (DPA-AFX 2000; DPA-AFX 2001; Hagelüken and Schumacher 2001)(*So far, I do not have any information regarding British union attitudes on this issue.*)

The only notable divergence of attitudes within the union camp concerns expectations regarding the effect of the takeover directive on worker consultation at the national level. Roger Lyons, secretary general of the Mining, Science, Finance Union in 1997 enthusiastically endorsed the EU takeover directive on the grounds that “[t]he non-statutory code in the UK sets the panel outside and above the law the UK courts generally refuse to intervene. Consequently, the rights of employees to consultation before mass redundancy announcements, provided for by EU directive, are flagrantly breached [...] A statutory EU-wide code would democratize the merger process, and perhaps dealings between bidders and target companies may come under the spotlight, even allowing for proper consultation with employee representatives, providing some test of fairness. [...]”(Lyons 1997). By contrast, German unions have tended to see legislative efforts on takeovers more as a potential threat to domestic codetermination arrangements. (DGB 2000; Handelsblatt 2001) This difference in

¹⁰ Employers in both countries, divided over the neutrality rule, are united in opposition to such proposals.

attitudes is clearly due to the differences in the pre-harmonization status quo in the two countries.

The investment banking community in both countries has favored the spread of liberal takeover rules. Some British bankers nurtured hopes that the removal of barriers to takeovers in other member states "could result in an increasing number of companies in Europe going public over the next decade. This may result in further business to be had." (Yerbury 1990) German corporate finance teams- largely based in London- reportedly also lobbied hard for the adoption of the directive "as they step up their attempts to generate more fee-rich European takeover activity"; (Murray 1999; see also Schubert 2001) Rolf Breuer, then chief executive of Deutsche Bank, criticized the German government for blocking the directive in 2001. (Wilson 2001)

Stockmarket authorities in both countries have also favoured harmonization along British lines. The British takeover panel, a non-statutory body under the umbrella of the Financial Services Authority has lobbied hard to maintain its self-regulatory status (e.g. Price 1997; Rice 1990; Whitebloom 1996) In Frankfurt, where plans about which body should be given responsibility for running takeover rules deriving from the directive were already underway in 1991, Rüdiger von Rosen, head of the stock exchange, expressed himself in favor of a self-regulatory system along British lines. (Dobie 1991b) The takeover panel has also campaigned strongly against moves to relax the neutrality rule. (Eaglesham and Solman 2001; Sabbagh 2001) The German Börsen-sachverständigen-kommission, responsible for rules of conduct in the case of mergers, echoed this view. (Hagelüken and Schumacher 2001)

The same applies to minority shareholders. The UK shareholder association UKSA stressed that it was "particularly concerned to retain the relative protection of the interests of private and minority shareholders provided by existing UK structures" and that it "would strongly oppose any reforms that weakened that protection". (UKSA 1997; see also UKSA 1994) German minority shareholder associations reportedly also opposed efforts to weaken the neutrality rule. (Rathbone 2001)

While it thus seems that, with the exception of employer federations, there is little variation in attitudes of similar groups across countries, the same cannot be said for the relative weight of similar groups in discussions surrounding the directive. I have not found a satisfactory quantitative measurement for this variable, but judging from the relative output of readily available position statements, it seems clear that the

British takeover panel has clearly been "among the most vociferous campaigners" (see Wheatcroft 2001), while German stock market regulators have barely made their voice heard. The opposite holds true for trade unions, with the British TUC largely tagging on to the position of the European Trade Union Federation (ETUC), while the DGB took a leading role. Industrial employers were more visibly mobilized in Germany, while the financial sector was more prominent in the UK. (*How can I prove this?*)

Summary and implications

As shown above, different political dynamics are at work in the two policy areas. British and German employer federations united in opposition against the EU-wide spread of "German-style" worker consultation, while unions in both countries were in favour. On the takeover directive, the German employer federations have joined forces with German unions to lobby against the spread of "British style" takeover rules, while the CBI has aligned with financial sector interests in order to promote it. Several lessons can be drawn from this.

First, it shows that functionalist "battle of the systems" explanations for the divergence of British and German government positions in EU negotiations over company law harmonization are unsatisfactory. It is clearly not the case that "interest groups and governments largely share a commitment to maximizing the comparative institutional advantages of their respective market economy." (Fioretos, 2001: 225) Instead of relative preference homogeneity based on a joint and stable vision of a common good, we see intense struggles at the domestic level between and within groups - sometimes even within governments- as well as preference changes over time.

The observed heterogeneity of preferences at the domestic level begs the question why these struggles play out differently across countries, as reflected in divergent government positions. The most straightforward explanation is that German governments since the late 1970s have paid more attention to union preferences than have British governments. Unlike German employers and British unions, German unions and British employers have systematically favored institutional choices conducive to the maintenance of their respective production regimes. The fact that

German employers have sided with unions on the takeover issue made the policy choice all the easier for German government.

Second, the fact that different political coalitions sustain the status quo in each policy area bodes ill for the future of the German model as depicted in the Varieties of Capitalism literature. In the long run, we should expect a decoupling of supposedly complementary arrangements due to divergent "temporal underpinnings" (Orren and Skowronek 2000) of the respective coalitions. The above discussion has shown that German employers cannot be relied upon to maintain the coherence of their "production regime" (if there is such a thing). They want to have their cake and eat it i.e. they want the insulation from takeovers of a coordinated production regime without the consultation requirements that supposedly go with it. This implies that, in case of a shift in the balance of power from unions to industrial employers, we should expect the dismantling of consultation rules, but not necessarily a facilitation of takeovers. A shift of power towards financial sector interests is likely to produce a more coherent move towards a liberal production regime.

The threat of future regime incoherence is amplified by the differential impact of economic downturns on the two policy areas. During downturns, the cross-class coalition against takeover liberalization is strengthened, because foreign takeovers are more likely and any job cuts potentially associated with them are more painful. At the same time, class-conflict over worker consultation intensifies as managers blame weak economic performance on their lack of flexibility.

So far, I have not found any strong countervailing mechanisms that would ensure a tight coupling or "elective affinity" between worker consultation and insulation from takeovers. (Except that German unions had more resources to monitor and lobby on takeover legislation, maybe partly thanks to funds earned through salaries of worker representatives on supervisory boards. But that seems a little contrived - even though a substantial part of the budget of the Hans-Böckler Stiftung does stem from that source. (Handelsblatt 2003c))

Even if such cross-policy feedback mechanisms did exist in the past, they are weakened by the increasing power of European decision-making bodies over economic institutional infrastructures. If two British Tories had not arrived late in the European Parliament on July 4, 2001, or if Britain and Spain had resolved their quarrel over Gibraltar before the Mannesmann takeover, the takeover directive would have passed, subjecting Germany to a more liberal takeover regime. Conversely,

British companies had to accept that their government's opt-out from the Maastricht Social Chapter did not save them from setting up European Works Councils for staff in their non-British subsidiaries. Due to the practical difficulties associated with excluding the British workers more than 90 per cent of companies affected ended up adopting "voluntarily" what they and their government had bitterly opposed. (Clement 1996; Lorenz and Smith 1994)

Third, comparison of the balance of power within countries across issues suggests that different mechanisms of institutional resilience are at work in the two policy areas. On the worker consultation issue, the relevant groups – workers and managers- exist in similar proportions in both liberal and coordinated market regimes and have similar preferences across countries despite the different institutional environments in which they are embedded. By contrast, each takeover regime creates its own constituencies. The most vocal defendants of the British takeover system – the takeover panel, the City of London, maybe also minority shareholder associations -do not exist to a comparable degree in the German context, while the group of potential victims (firms with undervalued stocks, large conglomerates, controlling minority shareholders) might be larger. Depending on the regime type, different groups prosper. In other words, in the takeover case more than in the worker consultation case, institutional choices in one round determine who is around to fight the next battle.

This would imply that different political strategies are necessary for successful institutional engineering in the two areas. In order to shift from one takeover regime to the other, massive political intervention is required only once. After that, internal tensions will gradually disappear as opponents to the regime wither away. With worker consultation, internal contestation persists and governments always have to act against the demands of sizeable part of the electorate in order to maintain a given regime.

Fourth, even though the cleavage structure in both policy areas allows the formation of coalitions across borders, the scope for using the EU as part of a two-level game to alter the balance of power at the domestic level is more limited than I had previously realized. Directives, the favored legislative instrument at the EU level, only set minimum standards to be complied with and leave national legislators to fill in the details. This means that German employers cannot directly achieve a reduction in consultation requirements within Germany by lobbying for low consultation

standards at the supranational level. Likewise, British managers do not automatically gain the right to use poison pills if they are permitted under the takeover directive, because their own government can choose to exceed the shareholder protection requirements laid down by the EU. Nevertheless, two-level strategies are viable in some instances. One example is the case of British unions, who have pinned their hope on European worker consultation directives to set minimum standards that constitute an improvement on their domestic status quo.

An interesting question that remains is *why* British and German employer federations adopted divergent positions on the takeover directive. Was it because British employers thought that they did not have any chance of prevailing against the City lobby to obtain an increase in takeover defences at home that they promoted their second-best alternative of a liberal level playing field across the EU? Or because financial sector interests prevail within the CBI? Or do British managers have less reason to fear a liberal takeover regime than do German managers, because, having already been subjected to it for some time, they are better adapted to it? (For example, the stock market valuation of British companies might more accurately reflect company value, or offer less potential for profitable restructuring, thus making them less attractive targets of hostile bids than German companies, some of which are arguably undervalued and/or overdiversified (see Goyer).

In this context, it might also be worthwhile thinking more systematically about general conditions for preference homogeneity within the employer camp. Why was cross-national unity among employers possible on worker consultation despite differences in the national status quo, while such differences led employers to pull in opposite directions on the takeover issue?

One answer may be that German employers have something to lose from spreading consultation to the rest of Europe even though they are stuck with it in their own country, whereas British managers have nothing to lose and something to gain from forcing managers in other countries to abolish the takeover defences that are illegal in the UK. German multinationals are affected directly by a spread of consultation to other countries and by the creation of European Works Councils because it forces them to also consult with workers in their foreign subsidiaries, which might not previously have enjoyed consultation rights. But even those German companies without foreign subsidiaries who resent strict consultation requirements at home might prefer not to spread them to the rest of Europe, because the existing

divergence makes it easier for them to counter German union demands for a further extension of consultation. It allows them to say “Look, you already have the most extensive participation in Europe. What more do you want?” or even “We will relocate if you don’t shut up.” No similar considerations are relevant in the takeover case.

Another explanation relates to the difference between liberalization and regulation. With takeover legislation, as with trade liberalization, the dismantling of barriers elsewhere is more important than at home. This means that the voluntary adoption option is not available quell intra-group dissent. With worker consultation, those companies who believe in consultation can adopt it whether or not it is mandatory, and they will earn more gratitude from their workers if it is not mandatory. (Like efficiency wages, consultation rights may be worth more to employers if they are not universal.) By contrast, a manager who likes hostile takeovers cannot simply adopt the rules of a liberal takeover regime for himself. She must strive for legislation in order to strip others of their defenses against takeovers, in particular those who are most attached to them.

To sum up, my empirical evidence suggests that functionalist "battle of the systems" explanations for divergent government positions are unsatisfactory because they neglect the political dimension of institutional design. Instead of relative preference homogeneity within countries based on a joint and stable vision of a common good, government positions reflect the result of struggles at the domestic level between and within competing groups. Moreover, different political dynamics are at work in the two policy areas. British and German employer federations united in opposition against the EU-wide spread of "German-style" worker consultation, while unions in both countries were in favour. On the takeover directive, the German employer federations have joined forces with German unions to lobby against the spread of "British style" takeover rules, while the CBI has aligned with financial sector interests in order to promote it. This has implications for theories on institutional complementarity, path dependence and two-level games and raises new questions about preference formation within employer federations.

The dissertation project which has given rise to the present paper is still at an early stage. Any comments regarding the empirical or theoretical parts would be much appreciated.

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ⁱ Germany's comparative advantage in "diversified quality production" (Streeck, 1991) is traced in part to the absence of takeover threats, which relieves managers of the need to constantly maximize shareholder value and reduces the possibility that existing governance coalitions are broken up through restructuring (Hall, 2001: 22; Höpner, 2001: 7; Franks, 1990, Porter, 1990). This is regarded as conducive to the building of long-term commitments between stakeholders, because it facilitates investment in human capital and makes it easier for companies to retain skilled workers during economic downturns.ⁱ Likewise, the German system of strong worker codetermination supposedly contributes to production strategies dependent on non-market forms of coordination, by providing employees with security against arbitrary layoffs, thus encouraging investment in company-specific skills (Hall and Soskice 2001; Streeck 1991; Thelen, 1991). Conversely, the British comparative institutional advantage in production strategies involving radical innovation is held to depend on ready access to venture capital and managers' ability to rapidly restructure production processes.

Rules preventing the free operation of stock markets or strengthening worker involvement in decision-making are seen as detrimental to the British production regime.