An Empirical Study of the Corporate Governance Effectiveness in the Czech Republic

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***Abstract*—**This paper aims to investigate the impact of corporate governance on financial performance in the Czech Republic. The relationships between board and ownership demographics and corporate performance were examined on a sample composed of 500 largest joint-stock companies from the processing and the construction industry. Correlation analysis and multivariate regression analysis were employed to test the sample on six hypotheses whose definitionswere based on similar studies from other countries.

The results of the analysis demonstrate apositive correlation between the company size and the size of its board. Among ownership demographics, a weak correlation between foreign ownership and firm performance was identified. Otherwise no potential link between any of the corporate governance demographic variables and the company performance was found in the Czech Republic.

***Keywords*—**Corporate Governance; Interlocking Directorates;Company Performance; Czech Republic.

I. Introduction

CORPORATEgovernance gained attention especially after the series of financial reporting scandals such as Enron, World.com in the United States or Parmalat in Europe. Since then, this issue has been analyzed in a number of theoretical and empirical studies.

One of the fundamental questions is whether there is a relationship between good corporate governance and financial performance. This relationship has been proven by many empirical studies (recently e.g. [1], [10]and [19]).

The research was conducted mainly in developed countries where companies are listed on the stock exchange and are obligated to follow an extensive set of rules and to disclose various information and reports. In the past several years the focus of academics has shifted to corporate governance issues in emerging economies around the world in order to explore and describe characteristics of partial countries. The objective of this paper is to proceed with this research and to evaluate corporate governance practice in the Czech Republic.

Companies in the Czech Republic are not required to publish any report concerning corporate governance and it is at their own discretion to follow the Czech Code of Corporate Governance based on the OECD Principles. Moreover, a number of public companies listed on the Czech capital market, represented by Prague Stock Exchange, are still insufficient to create a data sample for statistical analysis.

From the international point of view, the study of corporate governance is rather complicated. Due to various institutional, cultural and social environments, the system is usually at least slightly different from country to country. Therefore, it is appropriate to properly introduce the models of corporate governance which exist in various countries and affect the potential application of empirical evidence, from the individual countries in the international scale.

In this paper we address two areas of corporate governance agenda. The first area represents the structure of the governing body, and the second one the various issues related to ownership as the governance mechanism.

A. Board characteristics

Corporate governance may be defined as: “Procedures and processes according to which an organization is directed and controlled.” [2]. The governing body does not deal with daily operations of an organization because it is the management’s task. Its role and responsibility is to set up the organization’s strategic direction and oversee, monitor and control the management in the given direction.

Governance in the organization is executed through the two basic models: the one-tier and two-tier board system (also called unitary and dual board system). In the unitary board system the governing body is called the board of directors which is consists of execute and non-executive members. This system is worldwide predominant (e.g. USA, UK). While in the two-tier system there are two separate boards, a supervisory board for the non-executive members and a managing board for the executive members. The two-tier system can be found exclusively in the Continental Europe (e.g. Germany, Austria and the Czech Republic). The board

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system is usually set by the law but there are some countries where shareholders can decide which system to adopt (e.g. France, Japan, and Slovenia).

Under the Czech Commercial Code in the Czech Republic, there is a compulsory two-tier board system with the Managing Board and the Supervisory Board. The Managing Board as the executive body governs and represents the company, determines the company's objectives and policies, appoints the company's management and reports to the Supervisory Board and to the shareholders at the Shareholders Meeting.

The Supervisory Board is appointed by shareholders and oversees how the Managing Board exercises its range of powers and how the business activity of the company is conducted. One third of the supervisory board members must include employee representatives for joint stock companies having more than 50 employees.

In the one-tier model, there isnot an institutional separation between ownership control and company executive. A board of directors manages both functions. An ownership control is supposed to be performed by non-executive directors who generally do not have financial or personal stake in the company. In the classic model, the CEO and Chairman role can be held by the same person (so called CEO duality). In case of a dispersed ownership and dominant position CEO the non-executive directors who are nominated by CEO and approved by a general meeting cannot execute proper ownership control since they are controlled and dominated by CEO as a board chairman. Therefore, the main issue of the one-tier board system is to balance the CEO and chairman roles and strengthen ownership control. The basic step, which rapidly spreads in companies, is to separate both roles and to appoint independent, non-executive director as chairman. In accordance with this trend, companies try to increase a number of independent, non-executive directors in the board of directors and also in various supervisory committees which are nowadays typically composed of a majority of non-executive directors. A nominating committee should help to reduce the CEO influence on the appointment of executive and non-executive directors.

Oppositely, the two-tier board system distinguishes between above mentioned functions and separates them. The managing board, consisted fully of executive members, is responsible for the company executive while the supervisory board of non-executive members serves as monitoring body for majority owners. Although the one third of supervisory board is by the Czech law nominated by employees, a dominant owner is still able to hold the voting majority through the chairman, who is nominated by the owner and has a casting vote in the event of a deadlock at a meeting of board. In dependence on company articles, a managing board may be forced to gain approval from a supervisory board on certain occasions. By such means, a managing board is under the control of a supervisory board or rather owner. The main issue of the two-tier board system is to secure efficient collaboration between boards.

B. Ownership characteristics

Besides the governing body, there are several other monitoring mechanisms which help shareholders to overcome the conflict of interests originating from the separation of ownership and control [3].

In the countries, such as the Czech Republic that does not have an active market for corporate control, concentrated ownership plays an important role of the governance mechanism because blockholders are able to monitor the company management more efficiently than a group of minor shareholders. Concentrated ownership tends to reduce informational asymmetry thus lowering agency costs. Shleifer and Vishny [4] state that ownership concentration and performance are positively correlated.

C. Financial Performance/ Company Performance

In this paper company performance is represented by financial performance which is the predominant approach employed in the corporate governance research. There are several measures of financial performance basically divided to two groups: accounting-based and market-based measures.

Accounting-based measures are founded on historical reports and therefore reflect the past performancerather than contribute to strategic decision making for the future. The most common representative of this group is return on assets and return on equity (employed in e.g. [10], [13], [38], and [41]). On the other hand, market-based measures,such as market to book ratio, [43] and the most common Tobin´s Q ([25], [42]), do not count on book values but relate to the firm valuation by market.However, the majority of latest studies include representatives of both groups of financial performance to test the robustness of findings (e.g. [12], [39], and [40]).

Besides financial performance we may mention another approach to the performance measurement –a social performance that stems from the link between corporate governance and corporate social responsibility. It is based on the premise that good governance should be responsible for satisfying the needs of all important stakeholders and overseeing company.

II. Literature Review

Numerous empirical studies have described a statistically significant positive relationship between corporate governance and financial performance in developed countries. Over the past years, international corporate governance has been expanded on a perspective of emerging markets.

In the Eastern Asia the attention has shifted from Japan and its specific system to new economies such as China, Taiwan or South Korea. One of the board characteristics analyzed in the one-tier system is the CEO (Chief Executive Officer) duality. The study concerning this issue on the sample of 1974 publicly listed firms in Taiwan indicates that there is a negative relationship between CEO duality and firm performance. The results are consistent with the trend in the current corporate governance practices of separating the positions of board chairman and CEO [5].

The significant development of corporate governance is reported also from China. The findings show a positive relation between market valuation of listed companies and overall corporate governance practices [6].

At the end of the twentieth century, the privatization process in Central and Eastern Europe has attracted the attention of scholars, who have analyzed the transformation of state-owned enterprises to private companies, and examined the influence of ownership concentration and structure.

There is a lack of studies regarding the relationship between board structure and company performance, however, there are several studies conducted on the ownership issues ([7], [22], [37] and [14]).

For instance, Gruszczynski [8] examines the relationship between the corporate governance rating and the financial performance of listed companies in Poland. The study confirms that the level of corporate governance of listed companies is to some extent correlated with their financial performance. However, there is no strong evidence that the governance of Polish listed companies relies on their financial performance.

The researchers in the Czech Republic began to acknowledge the utmost importance of corporate governance and underline that Czech firms only adhere to basic corporate governance mechanisms and rules. According to Sediva [27], the implementation of the OECD Principles of Corporate Governance along with the reform of the Czech bankruptcy law create the right conditions for Czech firms to innovate their administration and management face to face with the financial crisis. The author also points out the biggest challenge for corporate governance research in the Czech Republic –the fact that the lack or low quality of data in the Czech environment complicates the analysis of relationship between good governance and company efficiency.

The study of Hrebicek at el. [28] is another example of recognition of corporate governance impact on performance of the company. The authors discuss the relationship between company performance and reporting its key performance indicators and the need to identify and quantify these indicators.

Kocmanova et al. [32] empirically analyze social performance indicators in the Czech manufacturing sector. The authors select on the basis of cluster analysis 8 out of the original 19 social indicators including the indicators of the corporate governance.

In conclusion, we affirm that in the Central and Eastern European countries that share a major transition of state-owned enterprises into private companies in the last two decades of the twentieth century, issues of corporate governance are starting to be gradually addressed.

III. Independent Variables

Our overall research objective is to review the empirical evidence concerning board characteristics and corporate performance in the Czech Republic in the light of alternative theories on the relationship between the board composition and corporate performance. The Czech Republic represents an interesting case study as it is an emerging market with the two-tier corporate governance system. It is challenging to design adequate methods to measure the relationship between the corporate governance and financial performance of companies.

A. Board Size and Financial Performance

It is a generally accepted fact that board size is growing with the company size. According to the resource dependence theory ([17]and [9]), the larger companies will have the greater need for resources and for that reason will require a larger board. Therefore, we hypothesize that:

Hypothesis 1: The size of the company is positively correlated with its managing and supervisory board size.

A larger board does not necessarily mean a better financial performance. Jensen [11] suggested that boards of directors with more than 8 directors will not perform effectively. Mintzberg [16] suggests that large and diverse boards are more easily manipulated by CEO.

Yermack [23] found a strong inverse association between the board size and the company value measured by Tobin´s Q in a sample of U.S. companies. Conyon and Peck [26] tested this inverse association in five European countries and evidence demonstrates generally negative effect of the board size on corporate performance. Coles et al. [21] confirms the existence of a U-shaped relation between Tobin´s Q and the board size, suggesting that either very small or very large boards are optimal. Thus large board size may be optimal for large or complex companies.

On the other hand, Dalton et al. [33] reports nonzero, positive relationship between the size of the board and financial performance.

Theoretically, every new board member may bring new connections and skills thus increasing the company performance, until a point is reached, where an oversized board is unable to communicate efficiently. This results in decision making problems. Managing boards in two-tier system are generally much smaller than boards of directors in predominantly analyzed one-tier system. In order to maintain a comparative perspective, we combined a number of both board members in the manner of one-tier board. Thus we hypothesize that:

Hypothesis 2: The size of the managing and supervisory board is positively correlated with the company performance.

Measure: The size of the managing and supervisory board was added into a single value representing the total number of seats in both company boards.

B. CEO and the Managing Board

The theory is not unified in terms of whether the same person should hold simultaneously both the CEO and the chairman role. According to the agency theory, such situation leads to a reduction of board monitoring effectiveness, because the CEO as the board chairman is controlling himself.

This is not an issue in two-tier system, in which the executive and non-executive roles are divided between managing and supervisory board. The question is whether a CEO should also be the chairman of the managing board. In the past, the common practice used to be that the managing board had a meeting once or twice a year and the CEO was delegated to appoint the top management. The membership of the CEO within the managing board improves the effectiveness of company governance, because the board is aware of the top management's activities. Therefore we hypothesize that:

Hypothesis 3: CEO being also a chairman of the Managing board has a positive influence on the company performance.

Measure: A dummy variable equals to 1 if a CEO is also a chairman of the Managing board and 0 otherwise.

C. Interlocks

An interlock occurs when a member of the supervisory or managing board simultaneously serve on more than one board. As mentioned earlier, resource dependence theory assumes that larger boards will be associated with better company performance. Consequently, we expect that larger boards involve higher number of interlocks which links the company to external resources. Large board with external connections is the important body for company contributing to resource needs (capital, information, and market access) and so improving company performance.

However, empirical results are not consistent. Loderer and Peyer [29] examine listed firms in Switzerland and conclude that the seat accumulation of board members is negatively related to firm value and also that a larger board size is associated with lower firm value. The authors presume that the reason is the conflict of interest, and the insufficient time board member can dedicate to duties of individual companies.

Perry and Peyer found further evidence that shareholders in Switzerland react negatively when executives, who hold prior directorships, accept additional outside director appointments. They, however, suggest that outside directorships for executives can enhance firm value, when the executive accepts a nomination to the board of a financial firm, the board of a company operating in the same two-digit SIC, or the board of a firm with greater relative growth opportunities [44].

Phan et al. [30] report a positive relationship between interlocks and firm performance of Singaporean publicly listed companies. The inter-industry interlocks are especially crucial and boards use them to reduce environmental uncertainty.

Pombo and Gutierrez [31] investigate the same relationship in Colombia and find that a degree of board interlocks is one of the key drivers of improved firm performance.

Hypothesis 4: Higher number of interlocks is positively correlated with financial performance.

Measure: Number representing shared board memberships between companies (e.g. a member of the board who at the same time sits in boards of two other companies adds two interlocks to the total number).

D. Ownership Concentration

The ownership structure in the Czech Republic is similar to the German model, which is characterized by a concentrated ownership. Since there is no active market for corporate control, concentrated ownership plays an important role in the corporate governance mechanism. Blockholders are able to monitor the company management more efficiently than a group of minor shareholders, to reduce informational asymmetry thus lowering agency costs. Shleifer and Vishny [21] state that ownership concentration and performance are positively correlated.

The results of the empirical studies are divergent when the majority of evidence is supporting the positive effect of concentrated ownership. For instance, Lehmann and Weigand [13] in their study of German companies conclude that a large shareholder does not necessarily improve the corporate performance, but ownership concentration significantly improves the ROA of listed companies. According to the meta-analysis of 33 studies by Sánchez-Ballesta and García-Meca [20], the effect is stronger in continental countries than in Anglo-Saxon countries, which is in accordance with the claim that the relation between ownership and financial performance is stronger in countries with lower levels of investor protection.

Claessens and Djankov [3] in their study of 706 Czech companies over the period between the years 1992-1997 conclude that more concentrated ownership is linked to higher company profitability. Therefore, we hypothesize that:

Hypothesis 5: The ownership concentration is positively correlated with financial performance.

Measure: The percentage of shares held by a controlling shareholder.

E. Foreign Ownership

The ownership structure may be as important as the ownership concentration regarding company performance. Frydman [7] examines the ownership effects on corporate performance of mid-sized companies in the Czech Republic, Hungary and Poland, and concludes that a foreign ownership brings a significant improvement of revenue performance, although its impact is no more significant than the one of domestic outsiders. A reason could be the sample period between the years 1990-1993, which was in the middle of the privatization process when the transfer of technological and managerial know-how from foreign owners may have required more time. Frydman [7] does not investigate ownership concentration, because all the companies in the sample were characterized by a single dominant shareholder. Pivovarsky [18] found that the concentration of ownership by foreign

Table 1 Matrix ofSpearman's rank correlation – highlighted values are relevant to the hypotheses testing

Variable	Mean	Std. Dev.	1	2	3	4	5	6	7	8
1 ROS	4.48%	8.67%	1							
2 Revenues	2.3bn	12.0bn	0.064	1						
3 Debt/Equity	2.083	13.186	-0.25**	-0.085	1					
4 Board Size	6.762	2.255	**0.102***	**0.223****	-0.088*	1				
5 CEO = Chairman	0.372	0.483	**0.107***	0.128**	-0.012	0.068	1			
6 Number of interlocks	3.450	6.712	**-0.021**	0.116**	-0.074	0.210**	-0.027	1		
7 Ownership concentration	85.040	24.759	**0.078**	0.194**	-0.046	-0.073	-0.025	0.104*	1	
8 Foreign ownership	0.302	0.459	**0.148****	0.292**	-0.093*	0.121**	0.015	-0.22**	0.280**	1

* $p < 0.05$ (one-tailed); ** $p < 0.01$ (one-tailed)

Source: authors' analysis

companies and banks in Ukraine is associated with better performance than that of domestic owners.

Overall, the foreign controlling shareholder may improve the company corporate governance practice and therefore we hypothesize that:

Hypothesis 6: The controlling foreign ownership is positively correlated with financial performance.

Measure: The controlling foreign ownership in the data set was represented by a dummy variable. Companies with a controlling domestic owner were assigned value of 0, while companies with a controlling foreign owner were assigned 1.

IV. Control Variables

In order to properly analyze the relationship between corporate governance and financial performance, it is necessary to involve the control variables which could strongly influence ROS, which was selected as the dependent variable. Since the data set consisted of only two industries, we preferred onecommonly used company factor to industry related variables (e.g.[10], [12], [15]and [25]).

A. *Debt/equity ratio*

Debt may represent an important corporate governance mechanism, because creditors monitor the manager's activities and managers are therefore discouraged to accept excessive debt financing for investments with high risk. Overall, debt financing may reduce agency costs and may improve company performance.

V. Dependent Variable

Initially, company performance was tested against the return on assets(ROA). The Czech accounts are unfortunately very noisy and especially ROA turned out to be a weak performance measure because of the irrelevance of the book value of assets in Czech companies. Often the cost of an asset was not close to market value at the time of acquisition, and due to a lack of write-downs assets maintain book value long after their productive value is gone.

For this reason the return on sales (ROS) was selected as the measure of the company performance. The ratio is defined as earnings before interest and taxes (EBIT) divided by sales. ROS is however an indicator of accounting-based measures which are generally criticized for theirdependency on historical data and so the results do not reflect the actual situation.

Hence, the majority of empirical studies involve also Tobin's Q as a dependent variable. Tobin's Q is a market-based measure of the company performance, related to its market value. This indictor is however not applicable in the Czech Republic as the vast majority of the companies in the data sample are not listed.

VI. Data Sample

Our hypotheses are examined on 500 largest joint-stock companies (sorted by revenues) from the two most significant industries in the Czech Republic, that means the processing and the construction industry. The two industries combined accounted for more than 45% of the national gross domestic product in 2011 [24].

Focus on a limited number of industries was preferred as it enables the comparison of variables. Different industries usually exhibit different levels of ROS for instance. Accounting for multiple heterogeneous industries is the subject of our further research.

It is a common practice that data sample for an empirical investigation of corporate governance consists of listed companies. There are, however, only 28 listed companies at the Prague Stock Exchange which would not be considered as a representative data sample. Few companies preferred being listed on a foreign stock exchange (such as NASDAQ or Warsaw Stock Exchange) rather than on Prague stock exchange which makes the comparison even more challenging.

There are no obligations related to corporate governance requested by the Prague Stock Exchange. Hence, it is fully in competence of companies whether they comply with good governance practices.

For the investigation purpose, publicly disclosed information from two local information sources in the Czech Republic were used: official government websiteoperated by

Ministry of the Interior of the Czech Republic(www.justice.cz)and database Magnus maintained by ČEKIA (www.cekia.cz).

VII. Empirical Results

The mean and the standard deviation for all variables in Table 1 reflectfew basic characteristicsof the data set. Average ROS of 4.48% exhibits large deviation of 8.67%, which points to a large heterogeneity of the sample in terms of the financial performance.

Average board size of the executive and the supervisory board combined is 6.76, which is slightly above the averageinthe UK (6.51) and Germany (6.33), calculated by Conyon and Muldoon [35]. The average number of interlocks per company is 3.45 with almost twofold standard deviation. The results of a statistical analysis performed on interlocking directorates in the Czech Republic were presented by Nowak [36].

CEO is also the chairman of the supervisory board in 37.2% of cases and about 30% companies in the data sample have a foreign majority owner. There is also a high average ownership concentration of 85%; the standard deviation of 24.75% implies a high variability in this measure.

For the deeper understanding of the data sample and in order to test the hypotheses, the correlation, regression, and interlock analysis were further performed.

A. Correlation Analysis

While Pearson's correlation is a statistical measure of the strength of a linear relationship between paired data, Spearman's correlation benchmarks monotonic relationship. The employment of Spearman's correlation is therefore more suitable for variables that are not linearly related and may notbe normally distributed. For this reason Spearman's rank correlation was used in this analysis.Its interpretation is similar to that of Pearsons(e.g. the closer ρ is to ±1 the stronger the monotonic relationship).

Values in the correlation matrix in Table 1 relevant to the test of six hypotheses introduced earlier in this paper are highlighted by a bold font. First, it ispossible to see a correlation of 0.223 between the board size and revenues. Since in the context of this paper revenues serve as a proxy for the company size, this would imply that larger companies tend to have larger board size and so Hypothesis 1 is supported.

A correlation of 0.148 between the ROS and the foreign ownership, with the p-value lower than 0.01,maystill be considered strong enough to support the Hypothesis 6 stating that the controlling foreign ownership is positively correlated with financial performance. Thus, the foreign controlling shareholder may indeed improve the company corporate governance practice.

Other highlighted correlation coefficients between the remaining four corporate governance variables (the size of board, CEO being the chairman of the managing board, the number of interlocks, and the ownership concentration) are close to zero with rather low significance and therefore cannot validate remaining hypotheses (H2–H5).

Besides the correlations relevant to the hypotheses testing, other interesting results can be found in Table 1. There is a correlation of 0.292 between the revenues and the foreign ownership. This suggests that larger Czech companies are more likely to be owned by a foreign entity. The correlation of 0.280 between the ownership concentration and the foreign ownership further imply thatforeign entities tend to have a larger share when being a majority owner, than domestic owners in the same position.

Foreign entities seem to prefer owning a larger portion in larger companies while domestic ownership is more dispersed. The two outcomes are reflected in the correlation between revenues and the ownership concentration (0.194).

A notable correlation also appears between the number of interlocks and the foreign ownership (ρ = -0.224).Thissupports the intuitive idea that foreign owners are less interlocked with the Czech companies in terms of shared board memberships. On the other hand, domestic owners have stronger incentives to be linked to more local companies.

Weak correlations between revenues and other variables in column 2 of the correlation matrix imply that larger companies might have more interlocks, more concentrated ownership and their CEO has a higher chance of being also a chairman of the executive board.

B. Regression Analysis

Furthermore, the multivariate regression analysis was performed with ROS as the dependent variable. Its output is displayed in Table 2. The five independent variables used in the regression analysis were the board size (BOS), the ownership concentration (OWC), the CEO being in the board of directors (CEO), the foreign ownership (FOW), and the number of interlocks (INT).Debt/equityratio (D/E) has also been included as a control variable.

R square equals 3.3%, which suggests that selected variables do not describe the variability in ROS.The main reason for variables CEO and FOW having the p-value below 0.05 is that they were both represented by a dummy variable.

Table 2 Multivariate Regression on ROS

Dependent: ROS	β	*Std. Error*	*t Stat*	*P-value*
Intercept	0.021	0.017	1.294	0.196
BOS	0.002	0.002	1.190	0.234
OWC	0.000	0.000	-0.378	0.706
CEO	0.016	0.008	2.029	0.043
FOW	0.022	0.009	2.372	0.018
INT	0.000	0.001	0.397	0.691
D/E	0.000	0.000	-1.546	0.123

Source: authors' analysis

C. Interlock Analysis

Larger companies tend to have more interlocks (see Table

Table 3 Interlocks and Company Performance

Sales in million CZK	Number of inter-locks	Avg per com-pany	Return on Sales	Number of inter-locks	Avg per com-pany
below 500	223	2.82	negative	218	2.91
500-750	343	2.72	0-1%	285	3.80
750-1,000	176	2.59	1-3%	503	5.47
1,000-1,500	223	2.82	3-5%	216	2.73
1,500-3,000	458	5.39	5-10%	236	2.48
over 3,000	302	4.79	over 10%	267	3.18

Source: authors' analysis

3). This finding is intuitive as the hypothesis 1 confirmed that larger companies tend to have larger boards thus increasingthe probability of interlocks. Correlation coefficient of 0.110 in table 1 may also support this idea.

This may occur because the directors of the largest corporations are undoubtedly successful people and other corporations would therefore naturally seek their advice and would rather have them on their board than men of less ability. This may also occur, however, because of factors unrelated to managerial ability. The director of a giant corporation has more personal influence with other companies, with potential investors, and with the government than the common man [34].

There is,however, no observable link between the financial performance of the company (measured by the return on sales) and the number of interlocks in Table 3.

VIII. Conclusion

Because of the lack of empirical studies addressing corporate governance in the Czech Republic, one of fundamental objectives of this paper was to locally test the corporate governance variables employed in the empirical studies from other countries.

However, the findings of this study do not fully support the hypotheses based on prior empirical evidences from other countries. Only Hypothesis 1, stating that the company size is positively correlated with its board size, has been supported. This hypothesis implies that larger companies tend to have larger board size that is in accordance with resource dependent theory and prior empirical studies.

A positive correlation between the returns on sales and the foreign ownership in our data sample supports the prior findings byFrydman from the Czech privatization period. The foreign controlling shareholder may indeed improve the company corporate governance practice.

Neither correlation analysis nor multivariate regression analysis could indicate any other potential link between the selected corporate governance variables and company performance measured as Returns on Sales. Due to overall high level of concentrated ownership in our sample followed by insignificant correlation, we cannot confirm Claessens and Djankov′s findings. The board characteristics based on prior studies do not seem to be a significant factor of company performance in the Czech Republic. It is an important finding as it provides a potential for a further research in the area of its reasoning.

It is necessary to stress that a majority of prior studies are not applicable in this case, as the conditions in the Czech Republic differ in two aspects.

First, the analyzed foreign countries have an active capital market and the data sample usually consists of listed public companies, but it was already mentioned, there are merely 29 public companies on the Prague Stock Exchange. The Czech private joint-stock companies are not obligated to disclose more than annual reports. It is therefore difficult to extract many important variables (such as the independency of board members) from publicly disclosed information.

Second, the Czech governance is based on two-tier board system as opposed to the prior research from foreign countries. This raises the question whether the employed board demographic variables are suitable for the two-tier system existing in the Czech Republic. The possibility stems from the very concept of each model as it is illustrated in the introduction.

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