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Did You Know?

10 FACTS ABOUT CORPORATE GOVERNANCE IN THE EUROPEAN UNION

01 **Did You Know....**that each EU Member State has issued corporate governance guidelines for listed companies?

In each EU Member State, there is a a corporate governance "code", for listed companies.[1] These codes generally require that companies comply with the behaviors they recommend or explain why they did not.

Listed companies in the EU must publish, as of next year, a discrete corporate governance statement either in their annual report or separately.[2] The corporate governance statement must refer to the code that is applied by the company and explain whether, and to what extent, the company complies with that code. The company also must describe the main features of its internal control and risk management systems, provide information on the composition and operations of the board, as well as on how shareholder rights can be exercised. The EU decided not to develop a Pan European Code but requires that listed companies publish a statement on CG in accordance with a country code.

02 **Did You Know....**that all Member States now require or recommend the presence of independent directors on supervisory boards?[3]

The requirement of independent directors on supervisory boards for all Member States is a positive step for corporate governance in the EU. However, some differences remain in the definition of independence.

The EC has put forth a recommended list of independence criteria for supervisory board directors.[4] The EC recommendations include that independent directors:

- should not be an executive or employee of the company
- should not receive significant additional remuneration to his/her non-executive director's fee
- should not represent the controlling shareholder

03 **Did You Know....**that the EC has adopted an accounting "equivalence mechanism" aimed at reducing bureaucracy for companies from non-EU countries looking to do business in the EU?[5]

Companies from a non-EU country with a set of accounting principles considered "equivalent" to International Financial Reporting Standards (IFRS), that want to invest in Europe would be permitted to use those accounting principles in Europe without being required to reconcile the books with IFRS. The move is another one by the EC aimed at eliminating costly and burdensome reconciliation requirements for businesses.

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1 See the list of codes and recommendations at: http://www.ecgi.de/codes/all_codes.php

2 Amendments to 4th and 7th Company Law Directives 2006/46/EC.

3 http://ec.europa.eu/internal_market/company/docs/independence/sec20071022_en.pdf

4 Recommendation on the role of non-executive supervisory directors, February 2005, and report on recommendation's application by Member States, February 2007.

5 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/20&format=HTML&aged=0&language=EN

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04 **Did You Know....**that the EC is encouraging Member States to create an electronic network for financial information on listed companies?[6]

Implementing this network will facilitate investors' access to historical information on companies' performance and financial position as well as on changes in major shareholdings. Internal Market and Services Commissioner Charlie McCreevy said: "Transparency of company information must be made easier and simpler. Investors need easy electronic access, through a single gateway, to financial information on listed companies across the EU."

05 **Did You Know.....**that the EC is reviewing the need for a more coherent approach to transparency for retail investment products?

An increasingly wide range of investment products are becoming available to retail investors across the EU. However, EU legislation imposes different rules on product disclosure and distribution, depending on the legal form of the product or the nature of the distributor. Concerns have been raised that these differences may result in risks to investors, for example as a result of inadequate product disclosures. The Commission published a call for evidence in 2007 on whether there is a need for a more coherent approach to disclosure and distribution rules for 'substitute' retail investment products.

06 **Did You Know....**that the EC has proposed ten "fast track actions" aimed at cutting unnecessary red tape for small businesses?

The Commission's plan[7] would simplify the business environment for SMEs in the areas of company law, accounting and auditing. The proposed measures would remove or reduce include administrative requirements that are considered outdated or excessive. The proposed changes range from eliminating the requirement for outside expert reports while preparing for mergers, simplifying disclosure requirements and reducing reporting and auditing requirements for SMEs.

07 **Did You Know....**that the EC is trying to create favorable conditions for the development of a European market for corporate control and takeovers?

Evidence shows that a healthy takeover market can address some corporate governance problems. Companies that are not well-run can be purchased and made more efficient and competitive. With this in mind, the European Commission implemented a Takeovers Directive[8] aimed at encouraging Europe-wide takeover regulation. Making such Europe-wide regulation has proven difficult so far, though, as laws on corporate ownership and control vary across Member States. However, the Directive has improved shareholders' rights, including those of minority shareholders.

6 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/07/1494&format=HTML&aged=0&language=EN&guiLanguage=fr
7 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/07/294&format=HTML&aged=1&language=EN&guiLanguage=en
8 http://ec.europa.eu/internal_market/company/docs/takeoverbids/2007-02-report_en.pdf

08 Did You Know....that the EU will not require member countries to establish "one share one vote" policies?

A policy of one share, one vote guarantees that voting rights in a company are equally distributed among all shareholders. While the idea of share-voting proportionality is a worthy one academic studies have not yet clearly shown whether there is a positive link between economic performance of companies and a one share one vote policy.[9]

"Existing EU legislation, the takeover bids directive, the 2006 amendments of the accounting directives and the transparency directive already contain ample provisions on transparency on deviations from one-share-one-vote," McCreevy said. These measures are still to deploy their effects in the future.

09 Did You Know....that the EC recommends that companies publish policies on director remuneration?

To best inform shareholders about the company's remuneration policy, the EC recommends[10] that companies provide the following:

- An annual statement of its remuneration policy. This statement should be posted on the company's website.
- The policy should be voted on by shareholders.
- The total remuneration and benefits granted to individual directors should be disclosed in annual accounts or the remuneration report.
- Share option plans or other incentive share-based schemes for directors should be subject to prior shareholder approval.

10 Did You Know....that the EC recently evaluated how well Member States have implemented its recommendations on director independence and remuneration?[11]

Many of the evaluation's results showed that the recommendations were indeed being implemented. All Member States require or recommend independent directors on boards, though not all have followed the Recommendation's guidance on criteria for independence. The review also found that a large majority of Member States have introduced high disclosure standards regarding remuneration of directors, and some require mandatory disclosure.

There is room for some States to improve, however. A significant number of Member States do not recommend that board committees should comprise a majority of independent directors or even require that independent directors be members of these committees. Also, few countries have introduced a shareholder vote on the remuneration report.

9 For more information, see "Lack of Proportionality Between Ownership and Control: Overview and Issues for Discussion." OECD November 2007. http://www.oecd.org/document/32/0,3343,en_2649_37439_39671008_1_1_1_37439,00.html

10 EC recommendation on the remuneration of directors. December 2004.

http://ec.europa.eu/internal_market/company/directors-remun/index_en.htm

11 Report on application of recommendation on role of non-executive or supervisory directors by Member States. February 2007. Report on application of recommendation on the remuneration of directors by Member States. July 2007.

http://ec.europa.eu/internal_market/company/independence/index_en.htm

http://ec.europa.eu/internal_market/company/directors-remun/index_en.htm

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About the Forum

OUR MISSION

Established in 1999, the Global Corporate Governance Forum is an IFC multi-donor trust fund facility located in the Corporate Governance and Capital Markets Advisory Department. Through its activities, the Forum aims to promote the private sector as an engine of growth, reduce the vulnerability of developing and transition economies to financial crises, and provide incentives to corporations to invest and perform efficiently in a socially responsible manner.

The Forum sponsors regional and local initiatives that address the corporate governance weaknesses of middle- and low-income countries in the context of broader national or regional economic reform.

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