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European Corporate Governance Codes and their Effectiveness

Eddy Wymeersch

Partner

European Bank for Reconstruction and Development

Co-sponsor KPMG

EUROPEAN CORPORATE CODES AND THEIR EFFECTIVENESS

EDDY WYMEERSCH[1]

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1. IMPLEMENTATION AND ENFORCEMENT OF CORPORATE GOVERNANCE CODES

1. The purpose of this chapter is to investigate the instruments adopted to support the implementation of the corporate governance codes in the European financial markets. It is based on comparative research of the practices in a selected number of Western European jurisdictions. The issue of the implementation of the corporate governance codes has received ample attention, both in studies ordered by the EU Commission[2] and in academic research in Europe and around the world[3] (Bajpai et al. 2005; Millstein et al. 2005; Wymeersch 2005; Mohd and Nariman 2007; Pietrancosta 2011). The formal degree of implementation, namely, the often high numbers of companies that in their corporate governance statement claimed to have implemented the applicable governance code, is not the direct subject of this investigation, but rather, the question as to whether attention is paid to non- implementation, or to nominal, implementation including formal explanations. A different but related question concerns the verification by national bodies of whether spurious explanations are further investigated and whether corrective action is requested or imposed. On the basis of this comparative overview, some conclusions can be drawn pointing towards improvements of implementation techniques, or even changes in the overall framework.

2. RELATIONSHIP OF THE CORPORATE GOVERNANCE CODES WITH THE LEGAL ENVIRONMENT

2. By way of introductory remark, attention should be paid to the nature of corporate governance codes and the framework within which they have been developed. There are considerable differences in this respect, from a purely self-regulatory instrument without any monitoring of its implementation, to a

2. Comparative Study Of Corporate Governance Codes Relevant to the European Union And Its Member States, January 2002, research undertaken by Weil Gotschall and Manges, LLP, European Association of Securities Dealers and European Corporate Governance Network, January 2002, available at http://ec.europa.eu/internal_market/company/docs/ corpgov/corp-gov-codes-rpt-part1_en.pdf; see also Berglöf and Claessen (2004) pointing to the complementarity of public and private tools of enforcement, stating that: 'political economy constraints resulting from the intermingling of business and politics, however, often prevent improvements in the general enforcement environment.'

3. See also for examples of the worldwide interest in effectiveness of corporate governance provisions in the Malaysia Code, Corporate Governance issues and enforcement activities of the Malaysian Corporate Regulators, February 2007, calling for stronger regulatory involvement in the absence of shareholders' action, www.clta.edu.au/professional/papers/conference 2007/2007AS _CGIEAMCR.pdf; cf. the Nigerian code. A similar trend can be seen in Nigeria: Odidison Omankhanlen, 'CBN urges SEC to enforce corporate governance code, November 2011, available at www.tribune.com.ng/index.php/money-market/31895-cbn-urges-sec-to-enforce-corporate-governance code.

regulation of public character with regulatory monitoring. These differences are deeply embedded in the economic and social framework within which these codes have been developed.

3. Implementation of corporate governance rules in Europe is very much linked to the existence of the corporate governance codes that have now been adopted in all European jurisdictions. They are based mainly on self-regulation, whereby the internal bodies of the company are expected to ensure that the company is run and that its internal bodies act in accordance not only with the rules of company law, but also with the governance code or its internal rules of organisation. The action is based on ex-ante implementation by the company itself, along with some ex- post pressure exercised by internal and external influences or decisions: e.g. shareholders in the Annual General Meeting (AGM) or as activist investors, pressure groups, the press, corporate governance commissions, securities regulators, to name but a few.

4. The relationship between company law and regulation and the legal environment has been changing recently under the pressure of the financial crisis, whereby a certain number of topics have been transferred from a self-regulatory code to a strictly legally binding provision. Particularly in the field of remuneration, the unwillingness voluntarily to upgrade, adopt and effectively implement the code provisions has led to legislative action in several states. This issue illustrates the oft- mentioned tension between the codes and the law, and the fear that over time the law would absorb much of the codes' substance, which is one of the drivers to improve on the content of the codes.

5. The meaning of a corporate governance code has to be read differently depending on the applicable legal framework within which these codes have to be placed: as the laws are quite – and increasingly – different, the role of codes, as a complementary source of conduct rules, varies substantially. The monitoring effort will also vary, but not necessarily proportionately. Linked to the insertion of the codes in the legal frame- work is the question whether the law takes into account the existence and the provisions of the code, and whether legal remedies may be attached to breaches of the codes. Here, again, the situation is quite diverse, at least, as far as case law is concerned.

6. In any case, one should mention that the overall corporate governance system cannot be judged on the mere provisions of the codes, and that usually very substantial governance conduct rules are laid down in the provisions of the Companies Act, or other legislation (especially financial regulation). The present analysis is limited to the governance codes.

7. Adoption of a corporate governance code has become mandatory on the basis of Article 46a of the Capital Requirements Directive (CRD) IV that in its amended reading states:

> A company whose securities are admitted to trading on a regulated market within the meaning of Article 4(1), point (14) of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments (1) shall include a corporate governance statement in its annual report. That statement shall be included as a specific section of the annual report and shall contain at least the following information:
>
> **(a)** a reference to:
>
> (i) the corporate governance code to which the company is subject, and/or
>
> (ii) the corporate governance code which the company may have voluntarily decided to apply, and/or
>
> (iii) all relevant information about the corporate governance practices applied beyond the requirements under national law. Where points (i) and (ii) apply, the company shall also

indicate where the relevant texts are publicly available; where point (iii) applies, the company shall make its corporate governance practices publicly available;

(b) to the extent to which a company, in accordance with national law, departs from a corporate governance code referred to under points (a)(i) or (ii), an explanation by the company as to which parts of the corporate governance code it departs from and the reasons for doing so. Where the company has decided not to apply any provisions of a corporate governance code referred to under points (a)(i) or (ii), it shall explain its reasons for doing so.

8. Most of the Member States had already developed a national corporate governance code before the transposition of this provision. As provided in the Directive, in some Member States companies are allowed to choose a code other than the national one. Depending on the national law, the companies publish a corporate governance statement in their annual report, or in a separate brochure. As part of the annual report, the statement may, according to national law, be subject to a review by the auditor (Bratton 2003; Bedard and Johnstone 2004; Coffee 2005; Wong 2005). This would normally not be the case for statements that are published separately (e.g. a corporate governance 'charter', as required in some Member States).

9. The Directive refers to the 'comply or explain' approach, requesting identification of the parts of the code where the company departs from it and, more importantly, the reasons for doing so. In principle, it does not request companies to detail the measures they have adopted to conform to the code, meaning that they can simply state that the code is fully implemented (see the practice in Germany). In practice, most companies elaborate on their implementation of the respective code provisions, even when they conform with the applicable code.

3. IMPLEMENTATION OF CORPORATE GOVERNANCE CODES

10. Before analysing enforcement of corporate governance codes, one should have a more precise view about how implementation takes place within the companies and how companies report it. As the codes deal with a wide range of subjects, some of the information is fairly traditional, historical or standardised, and may remain the same over several years. However, other information is more sensitive and needs to be reviewed on an annual basis; this revision would normally be prepared by the company secretary and reviewed by the chairman of the board. As part of the annual report, the statement will be approved by the board and submitted to the general meeting. The formal adoption of the reference to the corporate governance code and the approval of the corporate governance statement by the board are important aspects of the overall regime, raising the question as to whether these decisions aim merely at disclosure, or could lead to binding the company to the positions taken by the board. Case law has not been very supportive of that line of reasoning and generally has not held that the code is binding or that third parties could derive rights from it. The case in which the general meeting would adopt – and not merely take note of – the corporate governance statement has not been tried in practice; its impact would be all the more significant, as it might affect the relationship between the AGM, the shareholders and the board.

4. MEASURING IMPLEMENTATION OF CORPORATE GOVERNANCE CODES

11. Much attention has been paid to measuring the extent to which the provisions of the codes have been adopted – i.e. a formal reference is made to the applicable code – and implemented – i.e. the code's provisions are both applied or derogated from – as, in the latter case, an explanation is due. Elaborate statistics have been drawn up leading to the analysis of how many of the provisions have been applied, and in the case of derogations, how many explanations have been given. These statistics give an indication of the overall implementation and further specify to what extent specific provisions have been implemented. The statistical tables also give a good view of the way governance issues are dealt with in the different jurisdictions. However, in some states, alternative tables have been published indicating a noteworthy lower degree of implementation. This difference may point to a difference in perception, linked to the position of the body that makes the evaluation, e.g. the assessment by the corporate governance commission or by an investor protection association.[4]

12. As a large number of the codes' provisions really do not stir much debate, the degree of implementation would better be measured by reference to the more controversial provisions, most conspicuously those on remuneration. In the latter case, the degree of implementation has generally been considerably lower, leading in some states to legislative intervention. Obviously the self-regulatory instruments have not been able to ensure effectiveness of these provisions.

13. Implementation also raises the more important question as to whether the statement is a merely formal disclosure, or whether it corresponds to the actual conduct of the company. This remark addresses both cases where the company asserts full implementation and when it gives an explanation for derogatory conduct. Most statistical overviews do not probe very deeply into the matter, as researchers do not have investigatory powers, nor do they engage with the company's management in order to verify the information. Hence, there are some inherent limitations as to the verification of the veracity of the information disclosed.

14. Another handicap also mentioned by some governance studies is the case of meaningless explanations[5], whether boilerplate, information identical from year-to-year, or explanations that refer to specific circumstances that are, however, not further elaborated upon. Information of that type should be discarded as a valid 'explanation'. No cases have been reported where corporate governance statements have been deliberately false or misleading, but the hypothesis should not be excluded. In a broader context, false statements, on corporate governance or on any other subject, may lead to civil or criminal liability, depending on the national legislation. No cases specifically relating to corporate governance items have been found, and the causality requirement would probably bar any civil liability.

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4. See in the Netherlands the figures published by VEB (the Dutch Investors Association) in Effect, 2009, n. 26 42, available at www.veb.net; also VEB Effect, 2009, n. 26 42, nt. 4; cf. Portugal, Relatório anual sobre o governo das sociedades cotadas em Portugal 2009, Tabela IX, available at www.cmvm.pt.

5. According to one observer, this relates to about 30 per cent of the statement.

5. DRIVERS FOR IMPLEMENTATION

15. The implementation of the corporate governance codes, most of which are largely voluntary, takes place under internal and external pressure. Company boards normally feel strongly implicated in reporting their activity and that of the company, as it makes their action more credible and contributes to building confidence in the board and in the company's business. Boards have become more conscious of the importance of their role in this respect, organising specialised governance committees, being very elaborate on some aspects of the code, proceeding to self-assessment, and in some cases, external assessment. In Europe, only a handful of companies still seem to resist paying any attention to the governance matter. It is quite striking that adoption of the codes also takes place in companies with concentrated ownership.

16. The shareholders are the first addressees of these reports and determine their position – in votes, in trading policy – on the basis of the performance of the company, including its governance. In some jurisdictions, the auditors verify data in the reports. The investors, acting in the AGM, request good governance and focus on perceived weaknesses. Institutional investors, whose large blocks are often untradeable, have no choice but to enter into a more continuous dialogue. Activist investors pay attention to governance issues and have requested changes in governance practices. Very recently, investors have exercised pressure on management's remuneration within the non-binding 'say on pay' regime (Thomas et al. 2012; Cheffins and Thomas 2001)[6]

17. Some of the pressure originates from outside the company. The markets are important levers for requesting 'better' governance from companies and indirectly have been able to urge some important changes. The press and specialised media act as a conveyor belt for information to the market participants. Some firms publish corporate governance ratings, pretending that better ratings contribute to higher returns, a statement that enjoys much support in the advisory world, but for which hard empirical evidence seems rather controversial.

18. Last, but not least, is the action developed by governance commissions who, apart from drawing up the governance codes, in several states are also involved in monitoring, and/enforcing the corporate governance provisions. As illustrated in the overview below, there is a wide diversity of systems, structure and practices with respect to the way in which commissions deal with their relationship to listed companies to which the codes are applicable.

6. THE SCOPE

19. The corporate governance codes generally apply only to listed companies, defined as listed on a stock exchange, or on a multilateral trading facility. Most codes mention that their provisions may also serve as a source of inspiration for unlisted companies.

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6. See also Financial Stability Board, Implementing the FSB Principles for Sound Compensation Practices and their Implementation Standards, 13 June 2012 and the FSF Principles for Sound Compensation Practices, 2 April 2009.

20. The legal domicile of the company is generally used as the connecting factor, but some codes also take into consideration the place of trading. The European Corporate Governance Forum has issued a statement relating to the case where different codes would be applicable.[7]

21. The discussion about corporate governance codes has been largely superseded in the banking sector, where specific recommendations and, in the future, hard supervisory law provisions,[8] will govern the internal governance of the banks (Hopt and Wohlmannstetter 2011).

7. COMPARATIVE COUNTRY ANALYSIS

22. This analysis is based on the description of the corporate governance codes and their implementation practice in a selected number of European jurisdictions. It allows us to situate the codes on the background of the social and economic context in which they have been developed and reflects the concepts adopted by the respective business leaders. As will be further illustrated, there are significant differences between the codes and the context in which they function, which there- fore make a comparison difficult (Coombes and Wong 2004). Therefore it would be superficial to make a horizontal comparison between the different codes. The method followed here is a bottom-up comparison, country by country, as this allows us to position each code in its overall context, dealing, for example, with the nature of the code, the composition of the monitoring committees, the follow-up methods and the structure of the securities market, etc. The description is essentially based on publicly accessible information.

23. The countries compared have been selected on the basis of their prominent position in the corporate governance debate, and the accessibility of the materials in the original language. Moreover, they represent several governance models, i.e. one-or two-tier boards, concentrated or dispersed ownership, self- or public regulation, and similar differences. This selection also reflects the bias – and limitations – of the author, and does not indicate that other jurisdictions do not have a valid governance practice. The countries selected are:

- Austria,
- Belgium;
- Denmark;
- France;
- Germany;

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7. See European Corporate Governance Forum, Statement of the European Corporate Governance Forum on Cross-border issues of Corporate Governance Codes (2009), avail- able at www.ec.europa.eu.

8. See CRD IV, Proposal for a capital requirements directive, IV, art. 86 et seg.; the most recent version is the Council document, 11 May 2012, 9716/12. These provisions have been severely criticised by Winter (2012a).

- Italy;
- Luxembourg;
- The Netherlands;
- Portugal;
- Spain;
- Sweden;
- Switzerland;
- UK.

7.1. AUSTRIA

24. Austria adopted a corporate governance code in 2002, which was drawn up by the Austrian Corporate Governance Commission[9]. The commission was composed of a wide group of representatives of different stake- holders in the governance field[10]. Among them were two representatives of the financial regulator, FMA, and one representative of the government in charge of the capital market[11]. The code is updated every year, most recently in January 2012. The listing rules of the Vienna Stock Exchange oblige listed firms to adopt the code as a condition for access to the first segment of the market[12]. On the basis of the Enterprise Law[13], listed companies[14] are required to publish a corporate governance statement in which they designate a code that is generally applicable in Austria or in the market of listing, or to state the reasons for not applying any code. The law does not require companies to elaborate on the provisions of the code with which they comply, only to state the reasons for non-compliance with certain provisions. Information about composition of the supervisory and management board and their subcommittees and the way they function is mandatory. Also mandatory is a statement regarding the measures adopted to support the presence of women in these different boards[15].

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9. Österreichischen Arbeitskreises für Corporate Governance, available at www.corporate- governance.at. The code was drafted on the basis of proposals by the Institute of Austrian Auditors (IWP) and the Austrian Association for Financial Analysis and Asset Management (ÖVFA).

10. Academics, auditors, two members of the financial regulator FMA, one of the ministry, and further representatives of the investor associations, the stock exchange, listed companies and practising lawyers.

11. 'Regierungsbeauftragter für den Kapitalmarkt', see www.wienerborse.at/beginner/lexi con/18/876.

12. Companies have to subscribe to the code by a 'Verpflichtungserklärung'.

13. Art. 243b Unternehmensgesetzbuch.

14. Reference is made to listing of shares, but also to companies that only have other securities listed on the Stock exchange or on an MTF.

15. Art. 243b, § 2 Unternehmensgesetzbuch

25. The code consist of a very detailed questionnaire (76 questions) based on a 'comply or explain' technique. It is divided into three sections: L for the legal provisions, C for those that apply on a 'comply or explain' basis and R for the recommendations. Apart from the general provisions included in most codes, the code pays specific attention to the position of the shareholders, issues of conflict of interest and the position and role of the auditors.

26. No mention has been found concerning monitoring of the individual corporate governance statements.

7.2. BELGIUM

27. The Belgian corporate governance code was originally developed by the Corporate Governance Commission, as a non-governmental initiative, on the basis of an agreement between the principal employers' association, the Brussels Stock Exchange, and the securities regulator, which was reflected in its original composition. Since then its composition has been broadened to include the persons active in the Institute of Auditors, the Federation of Pension Funds and the Federation of Investment Clubs[16]. Since its original version of 2004, the code was updated in 2009, which is now the version that has been officially designated[17] as the code applicable to all listed companies pursuant to the Companies Act[18]. The code applies to companies with shares listed on a stock exchange, but is recommended as a reference for other companies. It is essentially based on a 'comply or explain' approach; however, since its original adoption an increasing number of provisions that were part of the code have been introduced into the law. Regarding certain aspects, the code calls for stricter requirements than those required by the law, also clarifying the substance of several of the requirements laid down in the law.

28. A substantial body of corporate governance rules is now laid down in the Companies Act, as amended by the 2010 'Corporate Governance law'[19] and other legal acts[20]. The law requires a substantial number of disclosures that are relevant from the corporate governance point of view, referring not only to the

16. It is composed of 23 members, several from industry, some academics, and persons from different professions.

17. Royal Decree, 6 June 2010 designates the Belgian Corporate Governance Code, December 2009, as the code of reference; available at www.corporategovernancecommittee.be.

18. Article 96 § 2 Companies Act, also referring to a series of additional information items. The same provision enables a governance code to be designated by Royal Decree of 6 June 2010

19. Law of 6 April 2010 'for the strengthening of good governance of listed companies and independent public sector companies, and modifying the regime of the banking and financial sector', or 'Wet tot versterking van het deugdelijk bestuur bij de genoteerde vennootschappen en de autonome overheidsbedrijven en tot wijziging van de regeling inzake het beroepsverbod in de bank- en financiële sector', B.S., 23 April 2010.

20. See the Act on Gender Diversity L. 28 July 2011, BS 31 August 2011, and art. 96 § 2 Companies Act; also in the financial sector, the provisions dealing with banks' governance and the implementing circulars, see art. 20 et seq. L. 22 March 1993 on the legal status and supervision of credit institutions, B.S., 19 April 1993

applicable code, but also to practices that go beyond the code requirements[21], making these disclosures mandatory.

29. This parallel set of rules has created some confusion, as both call for a corporate governance statement, but with a somewhat different con- tent[22]. Of course, only the Act is enforceable in court. The securities regulator, the FSMA, also acts to enforce the legal provisions within the context of its vetting of prospectuses, or reviewing some of the annual reports. It has, for example, held company directors to good governance practice, i.e. arguing that independent directors should not receive income-related remuneration (e.g. share options). Obviously this action has not been successful.

30. The monitoring of the implementation of the code takes place, according to the Preamble to the code, in:

> a combined monitoring system that relies on the board, the company's shareholders, the statutory auditor and the Banking, Finance and Insurance Commission (CBFA, now FSMA), as well as other possible mechanisms.

31. The code refers to the corporate governance charter that is posted on the company's website and contains the main elements of the company's policies in this respect, and the corporate governance statement that is part of the annual report, and contains, apart from a reference to the applicable code, a more factual analysis of the actual corporate governance practices. It is the latter that is also addressed in the Companies Act.

32. Statistical monitoring reports based on the 'corporate governance charter' and 'corporate governance statements' have been published by a consortium of VBO, the employers' organisation, and Guberna, the Institute of Directors, relating to the 20 companies that are part of the most important market index, the BEL 20. Grant Thornton has also published an overview of the corporate governance practices in Belgium, leading to comparable findings[23].

33. The FSMA has published analytical reports on compliance with the code, covering all companies that are listed on the exchange. The latest report was published in September 2011[24], relating to the 2010 corporate governance statements. From the comparison of these reports it appears that the degree of compliance is significantly higher for the 'BEL 20' companies – approaching 100 per cent – while in the wider group of listed companies and depending on the specific items, compliance is substantially lower, notwithstanding significant improvements[25].

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21. Article 96, §2, 1st al., Companies Act.

22. In fact, the 'Declaration of Good Governance' provided for in the law regroups some information items for which disclosure was already mandatory, but that has now been regrouped. Both documents must contain a remuneration report to be adopted by the companies, but that imposed by the law imposes some additional disclosures.

23. Grant Thornton, 'Corporate Governance Review 2011: Listed companies make progress in applying corporate governance regulation', available at www.grantthornton.be; see for comparison, Heidrick and Struggles, Challenging Board Performance, European Corporate Governance Report 2011, available at www.heidrick.com.

24. FSMA, 'Les premières déclarations de gouvernement d'entreprise: étude de suivi de l'Etude n° 38', Etudes et documents nr 40, available at www.corporategovernancecommittee.be.

25. Improvements particularly in the fields of risk management and internal controls.

34. In its 2011 report, the FSMA formulated a considerable number of recommendations to increase the level of compliance, particularly in the following fields: remuneration – now largely covered by the Companies Act – board evaluation, internal controls and risk management[26]. Is was found that the 'explain' approach was not always followed with sufficient strictness, in some cases being completely ignored. If certain provisions of the code are considered non-applicable, companies should state this explicitly, giving the relevant explanations, as otherwise it gives the impression that the company has complied. Remuneration continues to be a point of interest, and disclosure could be improved with respect to pensions, as this data was generally missing.

35. From both monitoring documents it appears that the follow-up practices are analysed from a more formal point of view, essentially evaluating whether the necessary explanations have been given, yet rarely criticising their substance. In some cases the FSMA reminds companies of their obligations on the basis of the new law.

36. The Corporate Governance Commission has also published a guide- line for a meaningful 'explain' approach[27].

37. The auditors are required to certify whether the annual report contains the disclosures that have been mandated by the law and correspond with the data in the annual accounts as have been certified by them[28]. They do not report on corporate governance issues in general.

38. Institutional investors who participate in listed companies rarely exercise significant corporate governance action (Van der Elst 2010; 2012). An attempt by an investor protection association to undertake activism through a specialised investment fund that owned shares in all Belgian listed companies has proved unsuccessful and was abandoned.

39. Belgian case law on the corporate governance code is limited to one decision, Fortis[29]. Fortis was a bi-national company, in the sense that the Fortis share consisted of two shares ('stapled shares'), one of the Belgian parent and one of the Dutch parent. In principle, both companies would have to concur. According to Dutch law, certain important decisions have to be submitted to the AGM of the Dutch company, while no similar provision exists on the Belgian side. In order to bridge this difference, the Fortis articles of incorporation contained a provision according to which the board would decide in accordance with the Fortis Governance Statement. This statement contained a provision providing for a requirement similar to that applicable under Dutch law. As a consequence, for identical matters a decision by the Belgian AGM would be required. In summary proceedings, the Court of Appeal of Brussels overruled the first instance judge and held that the transfer of the bank activities to a third party without the agreement of the share- holders was apparently 'seriously illegal' and could have been declared void. Therefore the court decided to suspend it, recognising that the statement has a certain legal force. However, the argument was not pursued in the case on the merits.

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26. Elements that are now part of the CG law of 6 April 2010, nt. 21, see art. 96 § 2, 3rd, Companies Code.

27. Corporate Governance Commission, 'The Corporate Governance Commission helps Companies to Draw Up a Meaningful "Explanation"', Press release, 14 February 2012.

28. Art. 144, § 6 Companies Act.

29. See Cass., 19 February 2010, Revue pratique des socie´te´s, 2009, nr. 7009, 421 and Court of Appeal, Brussels, 12 December 2008, Revue pratique des socie´te´s, 2009, nr. 7010, 432 and the comments by De Cordt (2009).

7.3. DENMARK

40. Denmark had first adopted corporate governance recommendations in December 2001, and the last revision to date was in 2010. The legal basis of the code is section 107b of the Financial Statements Act, declaring that the corporate governance statement will be part of the management review in the annual report. The code was drafted by the Committee for Corporate Governance[30], who recommended the code for adoption by the board of Nasdaq OMX, which implements the code in its listing rules. This commit- tee was originally composed of four prominent Danish personalities, while the present committee comprises 9 independent persons (Andersen 2004). The code is referred to as containing good practice provisions and is based on the 'comply or explain' approach[31].

41. The code pays ample attention to the relations of the company with its shareholders, especially the institutional shareholders, referring to the notion of 'active ownership' as mentioned in the EU recommendation of 30 April 2009[32]. It refers to the concept of wider stakeholdership. Strikingly, the code contains a provision on board neutrality in takeover cases[33] and other provisions dealing with the board's obligation. The code calls for a comprehensive corporate governance statement that takes a position on each of its items, and is part of the management report in the company's annual report. Publication on the company's website is a valid alternative. There is no updating during the year.

42. There is no monitoring of the code, except that the exchange assesses whether the explanations are understandable. But it is clearly stated that the exchange 'does not intend to assess whether the content of an explanation is good or bad'[34].

7.4. FRANCE

43. The monitoring of corporate governance rules in France should be looked at from multiple viewpoints; apart from the elaborate rules of company law, the monitoring action by the securities regulator[35] and the two main 'codes of conduct', one drawn up by the employers' organisations, a second by the asset management bodies, must both be integrated in the overall view. The securities market supervisor AMF (Autorité des Marchés Financiers) plays a very strong role, essentially at the regulatory and advisory level. The AMF has been mandated by law to evaluate corporate governance in general, irrespective of the source on which the provision or practice is based. The AMF sees its role as 'supportive of good corporate governance practices with a view of stimulating their

30. Komiteen for god Selskabsledelse'.

31. Section 107b and Rule 4.3 of the Rules for Issuers of Shares of Nasdaq OMX Copenhagen 1–7–2010.

32. Recommendation 2009/385, Preamble 10.

33. See the provisions in the Danish Companies Act.

34. www.corporategovernance.dk.

35. On the basis of art. L.621–18–3 of the Code monétaire et financier, the AMF has requested companies to publish an annual report on corporate governance.

adoption by issuing recommendations and analysis for further development[36]. On this basis, it has published 8 annual reports. In its most recent report, it assesses the compliance with the legal requirements and the way companies have dealt with the disclosure called for in the self-regulatory instruments. From this integrated approach, one can derive that, according to the AMF, the system has to be looked at as a whole, and that the self-regulatory provisions are partly in addition to, partly an extension of the legal requirements.

44. Several important corporate governance provisions have been introduced in the Companies Law, and in these last few years in the Code monétaire et financier, making the system based largely on hard law. The attention given to corporate governance issues has increasingly become a matter of application of the law and regulations. In its annual reports on governance, the AMF analyses both the implementation of the governance provisions and the evolution of practices by the listed companies, on the basis of which it criticises existing practices or formulates ‘recommendations’ which, without being legally binding, are expected to be followed. The AMF’s annual report mentions cases in which the recommendations were not followed,[37] each year repeating the recommendations that were made in the previous report.[38] The pressure for adoption of the recommendations is therefore not negligible. In addition, some recommendations propose changes, some of which go beyond the existing obligations.[39] Research studies on specific items, for example, on audit committees, or the functioning of the general meeting, have been undertaken by or under the auspices of the AMF. The latter work-stream extends the perspective to the role of the shareholders, although those were usually not addressed in these reports.

45. The AMF has been invited to give its opinion on matters of remuneration, on the role of the audit committee, the internal controls and risk management. The initiatives taken by the AMF to urge companies to strengthen and report on their risk policies[40] and the way these must be dealt with in financial reporting and in the annual accounts should be mentioned. However, the AMF does not seem to play an important role in the field of enforcing corporate governance rules.

46. In February 2012, the AMF published a report on the functioning of the general meeting of shareholders, focusing on the interaction between shareholders and issuers, the exercise of the voting rights, the functioning of the meeting with special attention for the bureau and the rules relating to the agreements with conflicting interests, the so-called ‘conventions réglementées’, i.e. the agreements between related parties.[41]The report contains conclusions on a certain number of changes in the Companies Law, in internal practice rules, or in rules concerning the auditors intervening in some of these procedures.

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36. “Faire état des bonnes pratiques des entreprises en matière de gouvernance et d’en favoriser le développement a travers la formulation de recommendations et de pistes de reflexion’ (AMF, Rapport sur le gouvernement d’entreprise et la rémuneration des dirigeants, December 2010, p.15) available at www.amf-france.org/documents/general/10249_1.pdf.

37. AMF 2011 Report, nt. 40 reports on self-evaluation of the board, and on the requirement to submit to the board the acceptance of board positions in other companies.

38. AMF 2011 Report, nt. 40

39. Ibid

40. AMF, ‘Recommendation de l’AMF sur les facteurs de risque’, 29 October 2009.

41. AMF 2012,‘Report of the Working Group on General Meetings of Shareholders of Listed Companies’, available at www.amf-france.org/documents/general/10334_1.pdf.

47. There are several soft law instruments relating to corporate governance in France: the main codes are the AFEP-Medef, applicable to the largest market capitalisations, and the Middle next code, for medium and small listed companies. In addition, one should mention the propositions of the Institut français des administrateurs. The AFG, or Association française de gestion financière, has issued recommendations addressed to the asset managers active in the field of investment funds.

48. The French corporate governance code (AFEP-Medef) is followed by almost all French companies trading on the French official market[42]. The code has been developed by two associations – the AFEP[43] and the Medef[44] – and was republished in a consolidated version in December 2008 to allow for the incorporation of the remuneration rules, representing about half of the code's provisions, the other half being dedicated to the composition and functioning of the board of directors. There is no mention of the relationship with shareholders, with statutory auditors, or with other stakeholders. The AFEP-Medef is the usual reference code called for by the law[45].

49. The code is based on a 'comply or explain' approach. In order to ensure its application, the two associations declare that they will analyse the information published by the companies that are part of the SBF 120, the index of the Société des bourses françaises. They add that if they determine that one of its recommendations is not applied, and this without sufficient explanation, they will submit the issue to the leadership of that company[46]. The findings from this action are published in an annual report, of which three have now been released[47]. The said reports analyse the different recommendations, giving statistical data about the options chosen by the companies, for example on the structure of the board, the number of directors, the number of directorships occupied by a director, or about gender diversity, providing an interesting image of the top French corporate world. The report also reproduces explanatory statements of companies that did not comply with the code's recommendations, giving an overview of the diversity of arguments used for diverging from the code. However, the report does not comment on the explanations given. Moreover, there is no evidence of follow-up action by the said two associations as far as non - compliance by these companies is concerned.

50. A third interesting player in the French corporate governance debate is the shareholders, especially the institutional shareholders, acting through the AFG, regrouping the collective and individual asset managers. The AFG has published a set of Recommendations on Corporate Governance[48]

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42. For the list, see 2010 Report AFEP-Medef, indicating that one French company did not apply the code (annex 2).

43. Association française des enterprises privées groups all major listed French companies. It was created in 1982. See www.journaldunet.com/economie/enquete/afep/afep.shtml.

44. Mouvement des entreprises de France is the largest employers' association, with 700,000 members, 50 per cent of which are SMEs.

45. Loi n°2008–649 du 3 juillet 2008 portant diverses dispositions d'adaptation du droit des sociétés au droit communautaire modifiant les articles L.225–37 et L.225–68 du code de commerce: 'Lorsqu'une société se réfère volontairement à un code de gouvernement d'entreprise élaboré par les organisations représentatives des entreprises, le rapport prévu au présent article précise également les dispositions qui ont été écartées et les raisons pour lesquelles elles l'ont été.'

46. www.code-afep-medef.com/la-mise-en-œuvre-des-preconisations.html.

47. See 2e Rapport annuel sur le code AFEP-Medef, application du code consolidé de gouvernement d'entreprise des sociétés cotées par les sociétés de l'indice SBF 120, exercice 2009, November 2010.

48. AFG, Recommendations on Corporate Governance, January 2012, at www.afg.asso.fr/index.php?option=com_content&view=article&id=98&Itemid=87&lang=en.

essentially dealing with the participation of asset managers in the general meetings of listed companies and indirectly addressing corporate governance issues that are submitted to a shareholder vote, such as the organisation of the board of directors and its responsibilities, their remuneration and particular resolutions in the AGM such as those dealing with anti-takeover measures. The indirect legal basis is a legal requirement[49] according to which asset managers should exercise the voting rights attached to their portfolio shares and, if they do not, should explain their position. The AMF's réglement général obliges asset managers to publish their voting policies, the votes cast and the reasons for negative votes or abstentions[50]. The AFG follows up the agendas for forthcoming general meetings along with its comments for its members ('alerts'), expressing criticism with respect to the motions proposed, or indicating how they should be evaluated on the basis of its recommendations.

51. In a 2012 publication, the AFG analyses the results of the votes cast in the general meetings and identifies some interesting trends (Pardo and Valli 2012). It thus reported on an increase in asset managers' participation in more than 80 per cent of the cases referring to AFG recommendations and alerts, while asset managers frequently engage with listed companies ahead of the AGM directly, or with the assistance of the AFG. The number of negative votes is quite considerable[51], especially addressing dilutive capital transactions and director appointments.

52. These AFG 'monitoring alerts'[52] deserve special mention: the AFG regularly publishes comments on forthcoming AGMs, especially highlighting proposals that run against their recommendations, or raise other governance issues. It is impossible to give an overview of the numerous alerts published each year[53]. For example, one alert relates to the appointment of an 'independent' director proposed for election although he holds a 9.9 per cent stake in the company, or to an anti-takeover device, under the form of double voting rights in a company where the functions of chairman and CEO are not separated, while there is only one independent director[54]. These alerts indicate to the AFG members and to the public where corporate governance issues lie and how they relate to the AFG recommendations, but without expressing a formal direction for voting. The alerts merely recall the legal obligation for French asset managers to exercise their

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49. Loi sécurité financière 2003, art. 533–22.

50. AMF, Réglement general, art. 314–100 et seq.; it is on this basis that AFG publishes a 'bilan des votes', see www.afg.asso.fr/index.php?option=com_content&view=article& id=106&Itemid=152&lang=fr.

51. In at least 80 per cent of French companies, the asset managers reportedly voted against at least one motion. The AFG publishes the following list of reasons for casting a negative vote: (1) dilutive equity financing transactions: capital increases without preemptive rights, capital increases with preference periods, debt issuance, etc. (29 per cent); (2) appointment of members to boards of directors or supervisory boards: percentage of inside directors, directorship appointments, etc. (23 per cent); (3) equity financing transactions considered to be anti-takeover measures: issuance of 'poison pill' warrants, share buybacks, etc. (14 per cent); (4) management and employee share- holding schemes: grants of bonus shares and stock options, executive remuneration, etc. (13 per cent); (5) approval of regulated agreements (11 per cent); (6) appointment and remuneration of statutory auditors (4 per cent); (7) changes to constitutional documents that impact negatively on shareholders' rights: multiple voting rights and limitations, amendments to articles of association, etc. (3 per cent); and (8) approval of financial statements and allocation of net income (3 per cent).

52. SBF 120 alerts emanating from a 'cellule de veille': see 'Programme de veille 2012 de gouvernement d'entreprise sur les sociétés du SBF120', available at www.afg.asso.fr/index.php?option=com_docman&task=cat_view&gid=499&Itemid=151&lang=en

53. Ten cases in 2011, and going back to 2001.

54. Circulaire N° 4 concernant Derichebourg (2012) can be cited as an example.

voting rights. In fact, the alerts implicitly indicate where the proposals diverge from normal governance practice.

53. Outside the strict framework of the exercise of voting rights, the AFG mentions the frequent instances in which asset managers contact issuers whether informing them about their general voting policies and governance standards, or their reasons for opposing certain resolutions, while on the other hand, companies sometimes consult asset managers – or the AFG – about controversial resolutions.

7.5. GERMANY

54. The German Corporate Governance code (Deutscher Corporate Governance Kodex) dating from February 2002, was developed by the German Corporate Governance Commission and is published in the Official Gazette. This Commission was installed in 2001 by the government (to be more precise, the Ministry of Justice), which appoints its members[55]. Membership is composed mainly of academics, business leaders and representatives of the stock exchange, and the asset management or investor protection associations. According to its charter, the purpose of the code is to strengthen the confidence of German and international investors in German business by making the German business organisation more trans- parent and understandable, especially as to the two-tier board structure. It also aimed at introducing more flexibility in German company regulation, as the law itself is mandatory[56].

55. The code is based on the concept underlying German corporate law that companies are run with a view of their continuity and the creation of added value on a sustainable basis. This concept is part of the market economy where the interests of the enterprise and its continuity takes precedence over the interest of the shareholders. The code has been revised several times; most recently amendments have been proposed to its 2012 version. The code is based on a three-pronged series of provisions:

- recommendations that are binding on a comply or explain basis;[57]
- suggestions[58] that are not binding and may be left aside without disclosure; and
- legal provisions that are per definition binding, and are reproduced for reasons of clarity.

56. The use of the code has been made obligatory by § 161 of the Companies Act (AktG) which implements Article 46a of the European IVth Directive (CRD IV), as amended. It applies to companies that are either listed or have other securities – such as bonds – traded on regulated markets, including multilateral trading facilities (MTFs). The said legal basis requires companies to deliver a compliance declaration (Entsprechenserklärung) that is published in the online version of the Official Gazette. Companies that fully comply with the code can merely state that they comply in full[59]; other companies

55. It is officially designated as the 'Regierungskommission'.

56. See § 23(4) AktG

57. Identified by using the term 'shall'.

58. Identified by using the term 'should' or 'can'.

59. See, e.g., the full compliance declaration by BWM, available at www.bmwgroup.com/bmwgroup_prod/d/0_0_www_bmwgroup_com/investor_relations/fakten_zum_unter

will have to explain with respect to which provisions they do not comply, sometimes limiting themselves to stating that they will not apply the provisions, or that the provision is not adapted to the company's situation. The statements relate to the past, and to the intention of the company for the near future, the latter not being binding.

57. The Commission does not engage in monitoring tasks, other than updating the code. The implementation is followed up by the Berlin Center of Corporate Governance, led by Professor Axel von Werder, who has published yearly analytical reports since 2003 (Von Werder and Talaulicar 2009)[60]. In particular, the 2012 report deals with the assessment of the code by the leaders of German listed companies on the basis of a survey of almost all companies (Von Werder and Bartz 2012). The survey indicates that the code is generally considered as 'negative'[61], while there are some items where the persons surveyed considered it particularly weak (provisions dealing with the cooperation between Vorstand and Aufsichtsrat).

58. There are a number of investor associations active in the field of protection of shareholders' rights[62], however, it appears that these do not play a prominent activist role[63]. The Vereinigung Institutionelle Privatanleger, or VIP (Association of Institutional Shareholders), supports ethical and Environmental, Social and Governance (ESG) objectives and has recently taken an activist position in a prominent case[64]. Some associations represent mainly the listed companies[65]; others are mostly

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nehmen/Entsprechenserklaerung_2011_DE.pdf or partial compliance by BASF, www. basf.com/group/corporate/de/investor-relations/corporate-governance/index, indicating that it complies almost fully with the non-mandatory provisions or 'suggestions'; but compare Deutsche Bank www.deutschebank.de/ir/de/download/Entsprechenserklaerung_25_Okt_2011.pdf, mentioning that it will maintain its internal approach to conflicts of interest notwithstanding a decision of the Frankfurt Court

60. See the reports 2003 to 2012 on www.bccg.tu-berlin.de/main/publikationen.htm. They have also been published in Der Betrieb.

61. The 'comply or explain' concept, or 'Regulierungskonzept' received a rather negative assess- ment: 'eine eindeutig negative Haltung zur Funktionalität des Kodexregimes', Survey, Der Betrieb, 2009, 872; from the industry side, too, questions have been raised about the usefulness of the code, as opposed to legal obligations: E. Voscherau, 'Anforderungen an Aufsichtsratsmitglieder', Deutsches Aktieninstitut am 26 Oktober 2010; Lufthansa Aufsichtsratschef Jürgen Weber 'Perspektiven der Corporate Governance in der nächsten Dekade' 64. Dt. Betriebswirtschafter-Tag, 29 September 2010.

62. Deutsche Schutzvereinigung für Wertpapierbesitz; Schutzgemeinschaft der Kapitalanleger.

63. See Corporate Governance-Kodex für Asset Management-Gesellschaften, 27 April 2005, www.dvfa.de/files/home/application/pdf/Kodex_CorpGov_AssetMmt.pdf. The code requires these companies to cast their vote; it refers to its 'comply or explain' basis.

64. According to its website: 'A number of investors, including the U.K.'s Hermes and German shareowner association VIP have filed a no-confidence motion against the Deutsche Bank Supervisory Board. Investor complaints include dissatisfaction over the board's succession planning for CEO Josef Ackermann as well as misaligned executive pay and a poor sustainability strategy'. See Reuters, 24 April 2012.

65. Deutsches Aktieninstitut, mainly representing the German listed companies; available at www.dai.de/internet/dai/dai-2-0.nsf/dai_startup_e.htm

concerned with specific ESG issues[66] or aim at improving the functioning of the supervisory boards[67].

59. The perspective of the state, and in particular, state funds as a major shareholder in nationalised banks, is new (Hopt 2009). It is also worth mentioning that several other corporate governance codes have been developed, for example, for family firms[68] or for firms in which the German state participates[69]. However, it has not been possible to assess their role.

60. The legal function of the code has been discussed in legal writings and has led to a number of court decisions (Gebhardt 2012). One of these relates to the validity of decisions of company bodies that run against one of the recommendations of the code. Generally speaking, one could state that liability would attach to untrue or incomplete statements, but not to the provisions of the codes as such. Companies should ensure that their governance statements are always up to date and justify their investors' reliance. Business leaders have shown real concern about this aspect of their liability (Von Werder and Bartz 2012).

61. A first Supreme Court decision[70] on the legal position of the German corporate governance code relates to Kirsch v. Deutsche Bank, where the latter and its chairman were sued on the basis of a public declaration of the chairman of the bank about its solvency. The bank had accepted responsibility for its chair's statement, but had not declared this fact in its corporate governance statement, nor the way the boards had dealt with it, although they were clearly obliged to do so on the basis of the code's conflicts of interest provisions. The Court decided that this omission was legally relevant, being an untrue statement about a significant item. It would make the decision of the general meeting concerning the discharge of liability voidable. The code is to be considered the expression of a general legal rule: although departures from it are allowed, in the present case, these are departures not from a specific rule, but from a general principle or norm that is expressed in the code's provision (Lutter 2011). The statement is comparable to a prospectus for issuing securities, where there is reasonable expectation that its content is true, and that the expectations raised will be founded upon.

62. The Court of Appeal of Munich[71] upheld the possibility of having the decision of the AGM set aside for violation of a code provision relating to the age limit of members of the Supervisory Board. The nullity of this decision – not decided for factual reasons – was justified by the fact that the company bodies had not adapted the governance statement, although the company had committed to do so, and shareholders would have been entitled to rely on it, implying that the statement had to be

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66. Dachverband der Kritischen Aktionärinnen und Aktionäre e.V., www.kritischeaktionaere.de/presse.html.

67. Vereinigung der Aufsichtsräte in Deutschland e.V. (VARD).

68. Governance Kodex für Familienunternehmen – Leitlinien für die verantwortungsvolle Führung von Familienunternehmen – (version 19 June 2010), available at www.intes-online.de/UserFiles/File/GovernanceKodexDeutsch.pdf.

69. Public Corporate Governance Kodex des Bundes (Public Kodex), Principles of Good Corporate Governance for Indirect or Direct Holdings of the Federation, available at bundesfinanzministerium.de/nn_39010/DE/Wirtschaft__und__Verwaltung/Bundesliegenschaften__und__Bundesbeteiligungen/Public__corporate______________governance______Kodex/AnlagePCGKengl,templateId=raw,property=publicationFile.pdf. These principles are declared to be applicable from 1 July 2009. They do not apply to listed companies.

70. BGH, 16 February 2009, II ZR 185/07.

71. OLG Munich, 6 August 2008, 7 U 5628/07

adapted for changes intervening during the year. But the decision could not be based on the formal provisions of the law sanctioning violation of it or of the company's charter, as the code is not a legal instrument, and not enacted by government, but consists merely of conduct of business rules.

7.6. ITALY

63. The corporate governance code (Codice di Autodisciplina)[72] has been developed by a Committee for Corporate Governance, composed of major business leaders, and supported by the main business organisations[73], including the associations for institutional investors and Borsa Italiana S.p.A. The committee is part of the organisation of the Italian Stock Exchange, which follows up the application of the code indicating, where necessary, possible improvements. The code can be viewed as an instrument for preparing companies for a stock exchange listing. Its latest version dates from December 2011.

64. The law provides that listed companies must publish in their management report a 'report on corporate governance and ownership structure', the content of which is determined in the law itself[74]. In the same report companies are required to give information with respect to the 'adoption of a corporate governance code of conduct issued by regulated stock exchange companies or trade associations'[75]. As a consequence, the Codice di Autodisciplina is now adopted by almost all listed Italian companies[76]. This statement is subject to a 'comply or explain' regime, as the company will have to give reasons for not adopting specific provisions of the code. The practices followed by the company 'over and above' the legal requirements also have to be stated[77].

65. The provisions of the code are divided into principles and criteria of application[78] that are binding on the companies that profess to respect the code on a 'comply or explain' basis. The code also provides comments, consisting of 'suggestions' that can be disregarded without explanation[79]. Companies are expected to publish a corporate governance statement, stating how the principles and

72. Corporate Governance Committee, Corporate Governance Code, December 2011 (latest version).

73. ABI, ANIA, Assonime, Confindustria and Assogestioni.

74. Article 123bis TUF, or Testo unico finanziaro.

75. Article 123bis(2) TUF

76. In fact, 95 per cent of listed companies, but 13 have expressly stated that they do not to adhere to the code, but give information about their own system of governance: see Assonime, Noti e Studi, 2012, § 2.1. In addition, 31 other companies have announced that they would not apply one or several of the code's provisions, especially those dealing with the independence of board members.

77. Article 123bis(2) TUF.

78. Criteri applicativi, explained as the recommended behaviour necessary for achieving the objectives of the code's principles.

79. They serve to illustrate the meaning of the principles and 'criteri applicativi' and someways for achieving the stated objectives.

criteria have been applied, or the reasons for not applying them. The committee declares that it will 'monitor' the implementation of the code[80].

66. Starting in 2001, Assonime (since 2004 with Emittenti Titoli) publishes a detailed report each year containing data and analysis regarding the compliance by Italian listed companies with the Corporate Governance Code[81]. These annual reports provide an in-depth analysis on their compliance with the code's most significant recommendations, but also discuss several recent regulatory issues, or take a position on questions of interpretation. The Assonime reports offer a valuable source of information and insight into the Italian governance system. These reports do not publish names of, nor can Assonime engage with, companies that have not implemented the code.

67. Despite the fact that the corporate governance statements and the remuneration reports are regulatory information[82], Consob, the market regulator, is mainly involved in enacting regulatory statements, but apparently not in the implementation of the code. Up to now the Corporate Governance Committee has not functioned as an enforcer of the code either. Recently the committee stated its intention to evaluate whether to reinforce the 'comply or explain' mechanism and its monitoring activity.

68. The code essentially pays ample attention to board issues, while data about the ownership structure also receive much attention (Bianchi et al. 2011). The code has been amended several times: in 2011 to introduce the rules on remuneration, while its December 2011 version incorporates different changes that have appeared over time and takes account of the needs of smaller listed companies. The new code has been streamlined and, at the same time, strengthened, with a view to increasing the effectiveness of the recommendations, thereby taking into account the most recent national and international best practices, notably with respect to the central position of the board of directors, including of its 'independent directors', the role of board committees and the strengthening of the internal control system.

69. In particular, the code focuses on the role and composition of the board and its internal committees, the independent directors, the remuneration regime and internal control and risk management. The content and transmission of information to Consob takes place partly in accordance with standardised tables, established in accordance with Consob's instructions[83]. Pursuant to a law of 2011, Consob has published guide- lines ensuring gender diversity in Italian listed companies[84]. A 2011 law has further limited the number of directorships an individual director can exercise in financial institutions[85]. The law provides that asset management companies must cast the votes for their

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80. The expression 'monitor' has been used in the introduction to the 2011 revision of the code.

81. See the latest report, 'Corporate Governance in Italy: Compliance with the CG Code and Related Party Transactions (2011)', available at www.assonime.it.

82. Article 113ter TUF, referring to the information viewed in Chapters I and II, Sections 1, I-bis, and V-bis of the same Title.

83. Consob, Regolamenti emittenti, Art. 100 – Composizione degli organi di amministrazione e controllo, direttore generale, pursuant L. 12 June 2011 nr. 120.

84. Article. 1 of Law number 120 of 12 July 2011 has revised the Consolidated Law on Finance (Art 147 and 148b) requiring the introduction of statutory provisions that can be reserved for the less-represented gender in the relevant bodies to a share of one-third of the board of directors.

85. Law No. 214/2011, entitled 'Protection of competition and personal cross-shareholdings in credit and financial markets,' bans executives from holding a board seat in more than one financial institution operating in the same sector or market.

portfolio companies[86]. Academic research has been undertaken on the role and influence of specific groups of institutional investors (Bianchi and Enriques 2001; Barucci and Cecacci 2005; Barucci and Falini 2005; Bianca 2008).

70. In an academic research study, the compliance issue has been investigated by Bianchi et al. (2011), concluding that there is a lower degree of compliance than officially stated. The latest Assonime and Emittenti Titoli analysis shows that the quality and quantity of disclosure are generally good, and that in recent years, transparency about the reasons for not adopting the code has improved. However, business leaders have called for independent monitoring, without specifying how this is to be achieved.

7.7. LUXEMBOURG

71. Luxembourg adopted its corporate governance recommendations in 2006[87], as part of the listing conditions imposed by the Luxembourg Stock Exchange, the latter conditions being approved by ministerial decree. The code was drawn up by a committee composed of members of listed companies, financial intermediaries and representatives of the exchange, with academic support from the Luxembourg law faculty. It applies to Luxembourg listed companies, while special attention is paid to companies with multiple listings that can freely follow stricter foreign conditions. Companies are expected to publish a ‘Governance Charter’ on their website and a ‘Governance Statement’ in their annual report.

72. The code is quite an elaborate document, composed of principles that must be applied, recommendations that call for a ‘comply or explain’ approach, and non-binding guidelines. The Stock Exchange ensures the adoption of the recommendation in the framework of its external checks on disclosures provided in the listing conditions, while substantive follow-up is referred to as the task of the shareholders. Mandatory disclosures fall under the monitoring of the financial supervisor, the CSSF, or ‘Commission de surveillance du secteur financier’.

7.8. THE NETHERLANDS

73. Corporate governance and the implementation of the applicable provisions, especially of the codes, has received ample attention in the Netherlands (McCahery and Vermeulen 2009).

7.8.1. The corporate governance code

74. The Dutch corporate governance practice is based on elaborated legal provisions, laid down in Book 2 of the Civil Code, and in a detailed corporate governance code, which built on previous

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86. Article. subs. 2, TUF (Consolidated Law on Finance or Legislative Decree No. 58 of 24 February 1998; Consolidated Law on Finance pursuant to Articles 8 and 21 of Law no. 52 of 6 February 1996.

87. The official name is Les dix Principes de gouvernance d’entreprise de la Bourse de Luxembourg, 2nd rev. edn 2009.

similar documents known as the Tabaksblat Code, although previous documents have also raised an early interest in the matter[88]. The present code dates from 2008 and is based on a two-fold layer distinguishing between principles and practice notes. The code has been designated by the ministry as the applicable code, as referred to in article 391(4) of the Companies Act[89], according to which it will decide on the 'actual value and usability' of the code[90]. The code is based on a 'comply or explain' approach. The self- regulatory provisions of the code are not subject to enforcement by the regulators, i.e. both the market regulator and the prudential regulator. But both are confronted with governance rules laid down in the respective EU prudential or market directives.

75. Corporate governance practice is well documented in the elaborate reports of the Monitoring Commission Corporate Governance, which has published its third assessment in this field. This commission was set up on 2 July 2009 by decision of the Cabinet[91] and is composed of seven members – business leaders, practising lawyers and academics, assisted by a secretariat composed of persons originating from the two ministries involved (finance and economy). The task of the Corporate Governance Commission has been described as 'drawing up an inventory, on an annual basis, about how and to what extent the provisions of the code have been implemented, and the identification of the gaps or imprecisions in the code; moreover the Commission will keep itself informed about the international developments in the field of corporate governance and this from a perspective of the convergence of the codes'.

76. The commission proceeds to a detailed review of the corporate governance statements published by the Dutch listed companies. This analysis gives rise to an elaborate number of findings, for example, with respect to the overall compliance rate[92], the progress realised since the previous report and specific comments whereby compliance is noted, in addition to insufficient compliance or lack of compliance.

77. The commission has refined the notion of 'comply or explain', distinguishing what is considered to refer to strict application of the code's requirements from compliance, referring both to application of the provision, as well as non-application with reasoned explanation. The monitoring reports identify the state of application, and mention the most significant provisions where explanations are given. The selection of the provisions to be commented upon change over time[93], depending on the commission's attention to a specific item.

78. The monitoring report identifies the cases of non-compliance, especially when no explanation is given, or when the explanation is insufficient. If the company states that the provision is not applied due to reasons specific to the firm, or that the provision will be decided on a case-by-case basis, this is considered non-compliance. The commission also points to the danger of standardised explanations that companies sometimes reproduce from each other[94], a bad habit, as the explanation should be firm specific. Also frequent are the transitory derogations, which are acceptable, although not for more than

88. This was the so-called Peeters Recommendations 1997, see www.ecgi.org/codes/docu ments/nl-peters_report.pdf.

89. Besluit, 20 maart 2009, Stb. 2009, 154

90. 'actualiteit en bruikbaarheid'

91. Besluit van 6 december 2004, gepubliceerd in Staatscourant nr. 241 van 14 december 2004.

92. See Monitoring Commission Corporate Governance, Report 2011, p. 24 e.s.

93. For the list see ibid., p. 19.

94. Ibid., p. 12 et seq.

one year. Explanations should be explicit, e.g., with respect to board evaluation, where the method of evaluation and the outcomes must be described. In some cases the commission proceeds to an interpretation of the code's provision[95].

79. Beyond these surveys the commission has developed techniques to incentivise companies to make progress in adopting the code, for example, by holding application meetings[96] with groups of directors, top managers and shareholders, calling attention to specific subjects and exchanging experiences. The report does not mention whether individual cases, especially shortcomings, are discussed in these meetings; however, due to their composition, this seems rather unlikely. Another type of meeting is those organised with the employers' associations, the main unions, the Association of Securities Issuers, the Association of Investors and of Accountants, and the two supervisory authorities. Engagement with the Parliament's Finance Committee was announced for 2012.

80. Under the heading of the AGM the commission has analysed the position of the institutional investors. The Dutch corporate governance code states that institutional investors should publish their voting policies, the implementation of these policies (on an annual basis) and how they have voted (on a quarterly basis). Eumedion's 'Best practice 7' requests its participants to use their voting rights in a well-considered manner and in line with their voting policies. See the next section.

7.8.2. Other corporate governance recommendations

7.8.2.1. Institutional investors: Other organisations have published corporate governance recommendations addressing issues from their specific point of view. Eumedion, which is the Dutch professional organisation of the large institutional investors, mainly pension funds and asset managers, has published 'Best Practices for Engaged Share Ownership'[97], which request members of Eumedion and other interested shareholders to engage actively with the investee companies and report on an 'apply or explain' basis[98]. The Eumedion secretariat monitors these management efforts on the basis of published annual reports of the member organisations and reports back about it in a report to the Eumedion board, parts of which are published.

81. As part of the guidance provided in the Best Practices document, a list of instruments have been identified reflecting a set of escalating steps in cases where differences of opinion have not been bridged between the institutional investor and the management of the investee. The list reproduced hereunder can be considered the standard set of instruments for investors to ensure that boards take appropriate account of their points of view.

82. Elements for a policy of this kind may include:

– writing a letter to the management and/or supervisory board in which the matters of concern are explained;

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95. E.g., is the payment of an exit premium in the case of a voluntary exit by a director a case of where the exit payment is not acceptable according to the Commission?: Monitoring Commission Corporate Governance, Report 2011, p. 11, or the holding period for a director's restricted shares, allowing for an exception for sales serving to financing the upfront tax burden, ibid., p. 14?

96. 'Nalevingsbijeenkomsten' or implementation meetings.

97. The Best Practices were adopted on 30 June 2011, available at www.eumedion.nl/en/public/knowledgenetwork/best-practices/best_practices-engaged-share-ownership.pdf.

98. See § 1.3 of the Best Practices, nt. 8

– holding additional meetings with the management and/or supervisory board, specifically to discuss matters of concern;

– holding meetings with other stakeholders, such as other shareholders, banks, creditors, the works council and non-governmental organisations (NGOs);

– expressing concerns in a shareholders' meeting;

– issuing a public statement;

– intervening jointly with other institutional investors on specific issues;

– requesting that certain subjects be placed on the agenda for the shareholders' meeting or asking that an extraordinary shareholders' meeting be convened;

– submitting one or more nominations for the appointment of a member of the management board and/or supervisory director as appropriate;

– taking legal action, when appropriate, such as initiating inquiry proceedings at the Enterprise Chamber of the Amsterdam Court of Appeal;

– selling the shares.

83. Eumedion also publishes position papers about specific issues; often recommendations are attached to these analyses. Several of these statements deal with remuneration issues, dividend policy and the acquisition of own shares[99] and usually go beyond the requirements of the general corporate governance code. Thus, the latest Principles on remuneration[100] stated that not only must the remuneration policy be approved by the AGM, but that the remuneration report, as drawn up by the supervisory board, and containing the individualised implementation of its general remuneration policy, should be submitted to the AGM for a 'vote', whereby this probably should not be read as a formal approval. In case the supervisory board would not do so, the shareholders could express their views, and specifically their dissatisfaction, in the context of other votes, especially as part of their decisions to grant discharge of liability to the members of the supervisory board.

84. Some institutional investors have created separate investment funds, where securities are located that form the basis for a more active approach to engagement and which can then be held for the longer term. Depending on their organisation, these separate funds may also help to resolve the conflicted situation, for example, related to receiving price-sensitive information.

7.8.2.2. Public investors: The Association of Securities Investors (Vereniging van Effectenbezitters, or VEB) is an 86-year-old association regrouping individual and corporate investors through investment clubs (352) and engaging in the defence of their rights. The VEB attends about 150 general meetings yearly, and engages in activist positions, the most visible part of which is the numerous lawsuits for mismanagement, market manipulation and the publication of misleading information. These highly visible suits have led to several of the leading decisions in the fields of investor protection and of corporate governance, as will be explained further. The VEB has a direct communication investors

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99. Recommendation 2009, 'Aanbevelingen inzake de machtiging tot inkoop van eigen aandelen en inzake de verantwoording over het dividendbeleid', available at www. eumedion.nl.

100. 'uitgangspunten', or assumptions

service with helpline, publishes regular information on investment funds, along with a rating of these funds, and has engaged in public action against sales fees. It has published a takeover code, containing some high-level principles[101] and corporate governance ratings, but the latter practice seems to have been discontinued.

7.8.2.3. Banks: As a consequence of the banking crisis, in 2010 a voluntary code was drawn up by the Dutch Bankers' Association (NVB) as the follow-up to the elaborate report of the Advisory Committee on the Future of Banks[102]. The code has been subscribed by the Netherlands licensed banks and aims at restoring public confidence in the banks after the crisis[103]. It contains several provisions about corporate governance, especially on composition and function of the supervisory board and the management board of banks, stressing the importance of risk management and the ethical conduct of banks. It requires banks to be 'managed carefully considering the interests of all of the parties involved in the bank, such as the bank's clients, its share- holders and its employees'.

85. The code is based on a 'comply or explain' approach and is followed up by an independent Monitoring Commission Banks, appointed by the NVB, in consultation with the Ministry of Finance. The first report of the Monitoring Commission identifies the progress in adopting the principles made, especially by the largest banks. The report is essentially descriptive and does not identify issues relevant to a specific bank. It openly mentions doubt about the self-regulatory approach, but considers that a conversion into hard law would be 'inopportune and premature'[104].

86. *Other governance codes* Thee are several other fields where voluntary governance codes have been developed, largely inspired by the ideas and principles in the main code for listed companies[105].

7.8.3. Dutch case law

87. Several significant decisions have been rendered by Dutch courts, including the Supreme Court, referring to corporate governance issues. Most of the cases were first brought before the Enterprise Chamber (Ondernemingskamer), a specialised chamber of the Amsterdam Court of Appeal, that has been charged by the Companies Act to deal with disputes between boards, shareholders and company employees. The Chamber has the right to determine enquiries in company matters and adopts the measures that are necessary to remedy the conclusions from these findings – essentially whether mismanagement has occurred. The powers of the Chamber are considerable and include the power to annul or suspend the decisions of any corporate body to replace, suspend, or even dismiss members of the supervisory board or the board of directors; to temporarily change the articles of association; to transfer shares to an administrator; and, if necessary, even to wind up the company[106]. Several decisions of the Enterprise Chamber have dealt

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101. VEB Annual Report 2010, p. 15.

102. See Adviescommissie Toekomst Banken: 'Naar Herstel van Vertrouwen', 2009, available at www.nvb.nl/publicaties/090407-web_rapport-adviescommissie_toekomst_banken_def. pdfen. www.nvb.nl/index.php?p=290335. The code is dated 9 September 2010.

103. It was mentioned that this initiative was adopted to avoid more intrusive government regulation.

104. Monitoring Commission Code Banks, Rapportage Implementatie Code Banken, December 2011, p. 8, available at: www.nvb.nl/code-banken/rapportage_implementatie_codebanken_dec2011.pdf.

105. See, e.g., for the hospital sector: Zorgbrede governance code, available at www.branche organisatieszorg.nl/governancecode_.

106. Article 2:356 Civil Code.

with corporate governance issues, the most recent referring to the principles of governance or to the code itself. These decisions are often quite complex; therefore, the following summary is limited to the statements of the courts that relate directly to corporate governance.

88. Several decisions relating to the relationship between the board – usually the supervisory board, common to the large Dutch listed companies – and the shareholders, usually contesting the decisions of the board that were considered contrary to their interests, and for which they deemed not to have been adequately informed, or not having submitted their decision for approval to the AGM. Most of the time the Enterprise Chamber held in favour of these claimants, but the decision was frequently overturned by the Supreme Court. In one of its leading decisions, the Court held that neither in company law, nor the changes to the company law then under consideration, nor the generally accepted views on corporate governance[107], could support be found for holding that the board must submit a proposal to the AGM for a private bid on a substantial part of the company's activities[108].

89. In the ABNAmro case concerning the sale of US-based LaSalle Bank, shareholders contested the sale of the bank solely by decision of the board, and not of the AGM. The Supreme Court – reversing the Enterprise Chamber's decision – decided that sufficient consultation had taken place and that the interests of all parties concerned had been sufficiently taken into account, in conformity with the preamble to the Tabaksblat Code. According to the Court, the latter expresses the commonly accepted view in Dutch law, and corresponds to the core company law notions of 'reasonableness and justice' applicable to all company decision making (art. 2.9 Civ. code), while the decision further met the criteria for the correct implementation of their duties by each director[109].

90. Neither on the basis of the law, nor of the articles of incorporation, does the AGM have an approval right or is the board obliged to consult the shareholders. According to the Supreme Court, the commonly accepted legal opinion as expressed in the corporate governance code does not lead to the conclusion that the board of a company is obliged to submit for shareholder approval or consultation a decision that is within the competency of the board on the mere ground that shareholders have an interest in selling their shares at the highest price[110]. In another passage, the Court held that the code's provision on the relationship between the Supervisory Board and the shareholders does not imply that the board should justify its decisions on the matter at hand[111].

91. In the Versatel case, decisions of a court-appointed provisional administrator were contested; the Supreme Court held that the powers of the administrator flow from the provisions of the law on the powers of the directors and from the provisions of the corporate governance code[112].

92. The ASMI[113] decision concerned the action of activist investors who wanted the company to change its strategy and spin off some of its activities. These shareholders had not succeeded in gaining

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107. The decision refers to the 1997 statement of the Peeters Commission, www.commissiecorporategovernance.nl/Commissie%20Peters, on which the company had com- mented in its annual report: 'Aanbevelingen voor goed bestuur, adequaat toezicht en het afleggen van verantwoording' in the report, 'Corporate Governance in Nederland'1997.

108. Hoge Raad (HR), 21 February 2003, Hollandsche Beton Group, decision AF1486, § 6.4.2.

109. HR, 9 July 2010, ABNAmro decision 09/04465 and 09/04512, § 4.4.2.

110. HR, July 2010, ABNAmro decision 09/04465 and 09/04512.

111. Ibid., § 4.5.1.

112. HR, 14 September 2007, Versatel § 4.3.

direct influence, as the company had adopted the so-called ‘continuity’ model whereby preference shares were held by a foundation and the directors were appointed on the binding proposition of the Supervisory Board, a proposition that could only be set aside by a two-thirds majority. The Enterprise Chamber considered that this governance structure was outdated and defensive and prevented shareholders from exercising any influence on its strategic decisions in the company due to its ‘closed position’. The Chamber ordered an inquiry on the protective construction.

93. On appeal, the Court annulled the decision of the Enterprise Chamber. It held that the Chamber’s analysis did not correspond to Dutch law, where the board is required to serve ‘the interests of the company and of the enterprise it runs’[114], and involves the interest of all stakeholders, inter alia, the shareholders. This view conforms to the provisions of the Tabaksblat Code, whish ‘expresses the commonly accepted legal opinion in the Netherlands and reflects the above mentioned legal concepts of “reasonableness and justice”’. It is up to the board to decide on the company’s strategy and on how far it involves consultations with the shareholders[115]. The arguments of the opposing shareholders were held to have been rejected on valid reasons. The Chamber did not find that certain provisions of the Code had not been met; instead, it took account of the fact that the company had promised to live up to the governance code in the future.

94. In the case of Begeman[116], a small company heading for market exit, the company had stated in its annual report that it would probably not meet the code’s requirements – among others, its provisions on conflicts of interest – and therefore had not published a governance statement in its annual report. Nevertheless, the Enterprise Chamber held that it should have applied the code’s provisions on conflicted directors, raising the double question about voluntary adherence to the code and its effects, even in the absence of adherence. The court deemed that the rules on conflicts of interest should nevertheless apply.

95. This short overview can be summarised as follows: corporate governance is often referred to in Dutch case law and is held to express some of the basic principles of Dutch company law. Violations of the codes as the basis for legal action have been attempted, but the attempts have not been successful before the Supreme Court, not because the code was rejected as a legal instrument – several times it was held to express the concepts underlying Dutch company law – but because the factual situation did reveal a violation of Dutch law, and that was sufficient for the Court. Logically the code’s provisions are sometimes cited in support of the analysis of Dutch company law in general. Although a comparison is difficult to make, one could put the code at the same level as case law, not legally binding, but a useful – and authoritative[117] – source of information on the substance of the law.

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113. HR, 9 September 2010, ‘Asmi’.

114. Article 2: Burgerlijk Wetboek

115. HR, 9 September 2010, Asmi § 4.4.1.

116. Enterprise Chamber, 28 December 2006, Begeman, § 3.7.

117. But this aspect does not appear from the decisions.

7.9. PORTUGAL

96. In Portugal, the Corporate Governance Recommendations are adopted and implemented by the securities regulator, the CMVM[118]. As they relate closely to some legal provisions, a consolidated document has been published indicating item by item the legal requirements and the additional recommendations of the CMVM[119]. Although based on the advice of representatives of the business community, the code is essentially a document generated and monitored by the CMVM. The 'comply or explain' basis does not prevent it from being a statement of a public authority: the obligation to state the applicable regime and the relatively high level of generality of the code point in the same direction. The adoption of the code[120] – which purportedly contains recommendations, not formal legal obligations[121]– was made mandatory in 2001, obliging companies, on a comply or explain basis, to express themselves on the state of compliance and the means put at work. The most recent requirement to date is formulated in the CMVM regulation 1–2010, requiring companies to implement the code or, in specific circumstances, a similar code, to state which recommendations have and have not been adopted and, if it is the case, to explain the reasons for the non-adoption of some of the recommendations. The model and the data to be included in the governance report are detailed in the elaborate annex to the regulation, from which companies can depart on the condition that they state their reasons and publish other relevant remarks. The CMVM verifies the effective compliance with the recommendations and the quality of the explanations given. If the company fails to report compliance with the code and/or to explain the reasons for not complying with some of the recommendations, the CMVM has the power to apply administrative sanctions to the company. In at least one case it has also imposed a fine in this context.

97. The verification process is divided into two parts: the first consists of a check of completeness of the disclosures in accordance with the legal requirements, leading to corrections or completion of information. At this stage, the CMVM verifies if every listed companies has (i) adopted one (the) corporate governance code, (ii) stated its compliance or non- compliance with each recommendation thereto, and (iii) explained the reason for not complying with some recommendations. In the second stage, a more in-depth analysis is undertaken and discussed with the companies during a hearing about differences between the CMVM's and the company's reading. Further individual meetings with the representatives of the company concerned may take place in order to 'convince' them about adherence to the recommendations. Compliance is finally assessed at the end of this process, aiming at urging companies to provide adequate and coherent explanations for not following the recommendation.

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118. The last update dates from 2010: CMVM Corporate Governance Code 2010 (Recommendations). Commercial organisations publish in-depth investigations with critical comments, but always on a no-name basis. For the text, seewww.cmvm.pt/EN/Recomendacao/Recomendacoes/Documents/2010consol.Corporate%20Governance%20Recommendations.2010.bbmm.pdfwww. cmvm.pt/EN/

119. Consolidation of the Legal Framework and Corporate Governance Code, www.cmvm.pt/EN/Recomendacao/Recomendacoes/Documents/20122010.Cons.MM.BB.Cons%20Fontes%20Norm%20%20e%20CGS%202010%20trad%20inglês.pdf.

120. Issuers may comply with a different corporate governance code instead. However, since there is no other Portuguese corporate governance code, the CMVM Code has been the only one adopted

121. The preamble refers to 'recommendations' but most of the code's obligations are formulated in the 'shall' mode.

98. The CMVM reports in detail on the outcomes of this process, holding a press conference where information is given about the most and the least compliant companies, also highlighting the better explanations. The most significant enforcement instrument, however, is the CMVM's annual report which publishes detailed nominative statements about the state of compliance.

99. The CMVM has closely studied the corporate governance publications and practices of the 49 Portuguese listed companies for several years. The last detailed overview of its corporate governance analysis deals with the statements for 2009[122], illustrating the considerable efforts in terms of staff and time that are invested in this matter. The overview publishes its assessments in a nominative way, indicating for each of the listed companies whether and to what extent the recommendations have been met. Rankings and score lists are established indicating the assessment gap, or the differences between the – usually more positive – assessment of each item by the company[123], and the separate assessment by the CMVM, distinguishing between the 'essential recommendations' and the 'other recommendations' and adding a column for a 'synthetic indicator' for total compliance. Aspects considered essential, such as the functioning of the general meeting, the position of the shareholders[124] and the recommendations on the boards are further explored, while several other, more sensitive recommendations, such as the recommendation on remuneration, are individually analysed. All of this information is given per company, indicating in suggestive colours which company has been deficient in a specific class of recommendations. The table relating to the 'remunerations' particularly shows much more 'black' than the tables for the other recommendations, indicating a poor degree of implementation.

100. On the assessment of the 'comply or explain' practice, the report identifies the main items of concern: anti-takeover protections[125], provisions on the designation, evaluation and dismissal of the auditor, remuneration rules and the provisions relating to alignment of shareholders' and directors' interests. All of these are fields in which, according to the report, the compliance rate is significantly lower than the average compliance. Although the report extensively uses the 'name and shame' instrument by identifying non-compliant companies, the judgment is sometimes a balanced one: e.g. in the case of Portugal Telecom, where the company had refused to abandon its anti-takeover defences, the draftsperson of the report stated that he saw no arguments for condemning the company's position. Non-compliance leads to individual meetings with the companies concerned in order to 'convince' them about adherence to the recommendations.

101. The Portuguese regime is specific in the sense that it comes close to a full regulatory regime, although still based on a 'comply or explain' technique. It is unclear to what extent the CMVM imposes its views and whether the 'explain' view, provided it is adequately motivated, prevails. Since 2009, the CMVM has stepped up its monitoring efforts, proceeding to a more thorough analysis of the level and quality of explanations.

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122. Relatório anual sobre o governo das sociedades cotadas em Portugal 2009, available at www.cmvm.pt/CMVM/Estudos/Pages/20110519a.aspx.

123. Often due to a more optimistic reading of the Recommendation, according to the CMVM.

124. E.g., the recommendation in favour of 'one share, one vote'.

125. As the Recommendations contain a statement in favour of 'one share, one vote', remarks are addressed to limits on voting rights, protective charter provisions, or quorum requirements

7.10. SPAIN

102. On the basis of a Securities and Markets law of 1988[126], a decree[127] has delegated to the CNMV, the Spanish securities regulator, the power to define the content and form of the annual report, including the corporate governance statements. The decree contains a fairly elaborate list of items to be included in the CNMV's implementation document, the 'Unified Code'[128]. On the basis of this decree, it is responsible for drawing up not only the code, starting from the two previous codes[129], but also for exercising surveillance on its application[130]. In July 2005, a Special Working Group was designated to assist the CNMV in drafting the code, in close consultation with the private industry and the Ministries of the Economy and of Justice and the Central Bank. The Unified Code was adopted by the CNMV on 19 May 2006, and adapted to include remuneration provisions in 2009. In its annual reports for 2009 and 2010, the CNMV explains in detail the action it has developed to ensure effectiveness of the Unified Code, and other provisions affecting company life. The code is based on a 'comply or explain' method, against the background of the applicable legal provisions, among them the accounting rules that call for close scrutiny from the CNMV. According to the code:

> It will be left to shareholders, investors and the markets in general to evaluate the explanations companies give of their degree of compliance with Code recommendations.

In other words, the extent of compliance or the quality of explanations will not give rise to any action by the CNMV, as this would directly invalidate the voluntary nature of the code. This affirmation is under- stood to be without prejudice to the monitoring powers assigned to the CNMV with regard to the Annual Corporate Governance Report of listed companies in article 116 of the Securities Market Law and related Order[131]. This statement underlines the double nature of the Spanish code: it is not a purely self-regulatory document, but has been elaborated by the CNMV and is applicable on the basis of a legal provision. Moreover, the CNMV closely monitors the way the code is applied, as will be illustrated below.

103. The CNMV has developed an elaborate practice relating to implementation of the corporate governance rules, as laid down in the code. This action is based on its general competence to verify the disclosures in the annual reports made by listed companies. It goes along with an equally important action in the field of accounting by listed companies. Both are commented upon in some detail in the CNMV's annual reports.

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126. Article 116 of the Ley 24/1988, de 28 de julio, del Mercado de Valores, modified by Ley 26/2003, de 17 de julio.

127. Ordinance ECO/3722/2003, of 26 December 2003, 'sobre el informe anual de gobierno corporativo y otros instrumentos de información de las sociedades anónimas cotizadas y otras entidades', noticias.juridicas.com/base_datos/Privado/o3722–2003-eco.htm.

128. Special Working Group, Unified Code on Good Corporate Governance, January 2006.

129. 'La Comisión Nacional del Mercado de Valores queda habilitada para dictar las disposiciones necesarias para desarrollar, en el ejercicio de las competencias que le son propias, lo dispuesto en la presente Orden'

130. Se faculta a la Comisión Nacional del Mercado de Valores para determinar las especificaciones técnicas y jurídicas, y la información que las sociedades anónimas cotizadas han de incluir en la página web, con arreglo a lo establecido en el resente apartado Cuarto de esta Orden

131. Whereby the CNMV may order companies to make good any omissions of false or misleading data.

104. In its first annual report since the entry into force of the new regime (2009)[132], the CNMV noted in 53.2 per cent of the cases factual non- compliance, a mere mention of the existence of a deviation without explaining the reason, or general disagreement with the recommendation. On the basis of this finding, the Commission has sent out deficiency letters that have led to changes in the disclosures, to rectifications and expansion of previous disclosures. Special attention was drawn to the qualification of independent directors, on which a table of possible grounds for lack of independence is established, and to related party transactions.

105. The annual report for 2010 shows a significant increase in terms of reporting of supervisory action. In the context of its oversight on financial reporting, this report calls for special attention to issues of internal controls and risk-management systems, as mandated by a change in the law[133]. Already in previous years, the CNMV strongly focused on accounting issues, especially on the basis of auditors' reports. The analysis gives a detailed analysis of the number of cases where qualified. reports were delivered and the types of shortcomings that were identified by the auditors. It also proceeds to a 'substantive review' of a number of accounts of companies, selected on a risk and random basis and resulting in 'deficiency letters' asking for additional information on accounting policies and information breakdowns[134]. Worth mentioning is the significant number of letters relating to accounting policies, specifically on valuation, related party transactions, impairments, etc. On that basis, the CNMV can require additional information, reconciliations, corrections and, in material cases, entire restatements.

106. In the corporate governance field, apart from statistical information on general compliance with the different provisions of the Unified Code[135], the CNMV's report gives statistics on board composition, remuneration, general meetings, etc.[136] With respect to the 'comply or explain' principle, the CNMV investigates cases where compliance was deficient, too generic or redundant, requesting further information or clarifications. These may result in further information, amendments, new information or additional explanations in 'explain' cases. Some of this information is included in the centralised company information database, organised by the CNMV.

107. Special action relates to independence criteria as laid down in the Unified Code: in case of doubt, 'deficiency' letters are sent for clarification or modifications. The type of violations are reported on. For example. In 2010 the number of cases where independent directors had 'significant business relationships' was quite substantial, but as far as one can derive from public documents, this did not lead to any additional information, nor to corrective action.

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132. CNMV Informe Annual de Gobierno Corporativo de las companies del IBEX 35, 2009, available at www.cnmv.es/DocPortal/Publicaciones/Informes/IAGC_IBEX_09.pdf.

133. Implementation of the Law of 4 March 2011, L1/2011

134. See CNMV, Annual Report 2009, Deficiency Letter on Independent Directors, p. 140.

135. For 2009, the 2010 Annual Report found full compliance in 77 per cent of the cases with the recommendations and 10 per cent partial compliance, especially on remuneration

136. Detailed information can be found in a separate publication, published annually: Informe de Gobierno Corporativo de las entidades emisoras de valores admitidos a negociación en mercado secundarios oficiales, last issue 2012, available at www.cnmv. es/portal/Publicaciones/PublicacionesGN.aspx?id=21.

108. The report contains detailed tables on related party transactions[137], stating the amounts involved and the variations vis-à-vis a previous period. Here again, the role of the CNMV is to ensure transparency. There is no indication that these disclosures have led to action by the CNMV such as criticising certain intra-company transactions or transfers to shareholders.

7.11. SWEDEN

109. The Swedish Corporate Governance Code was first adopted in 2005, and updated in 2010[138]. The code is drafted by the Swedish Corporate Governance Board, which is part of the 'Association of Generally Accepted Principles in the Securities Market', a body composed of members of the Swedish private corporate sector organised among the ten leading business associations. The Association itself is composed of three self-regulatory bodies: the Swedish Securities Council, created in 2005, in charge of overseeing self regulation in the securities market and formulating 'Good practice in the Swedish securities market', the Swedish Financial Reporting Board, and the Corporate Governance Board. Respecting these good practices is part of the listing agreement[139]. The Council – and not the Board – gives opinions on issues of interpretation of the code.

110. The code is a fully self-regulatory body of rules, applicable to all companies that have their shares or depositary receipts listed on one of the Swedish regulated markets[140]. It applies in addition to the Companies Act, containing an increasing number of formerly code provisions (Unger 2006). The Swedish Annual Accounts Act requires companies with their shares, warrants or bonds listed on a regulated market to publish a corporate governance report[141]. Except for a limited number of provisions in the Annual Accounts Act, the content requirements are laid down in the code.

111. The requirement to adopt the code is laid down in the stock exchange rules, and the exchange verifies whether the code is applied (Von Haartman 2010)[142]. It could take disciplinary action in the case of a serious breach which the company is unwilling to correct[143], but usually a dialogue will suffice. In principle, the board states that it is up to the markets and the investors to judge the quality of the information, while the exchange verifies whether the information is such that readers understand the reasons for non-compliance and what alternative solutions have been put forward.

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137. Subdivided in transactions with significant shareholders, persons or companies belonging to the group, directors and executives and other related parties. The table also includes regular flows, e.g. due to provisions of goods or services, dividends, licence agreements and similar items

138. The latest version to date: 'The Swedish Corporate Governance Code', 2010, available at www.corporategovernanceboard.se.

139. See Nasdaq OMX Stockholm AB's and Nordic Growth Market NGM AB's respective rulebook for issuers.

140. Nasdaq OMX Stockholm and NGM Equity.

141. Annual Accounts Act 1995:1554, chapter 6, ss. 6–9 and chapter 7 s. 31.

142. Fifty per cent of the companies follow the code without variation; another 40 per cent with one explanation, the remainder with more than one.

143. One case has been reported.

112. The Board publishes an annual report, in which it states its general approach to governance, expressing its firm belief in the Swedish company model with dominant shareholders. It publishes detailed data about the way the code has been applied in the most recent year, comparing it with data from the previous years. The code being based on 'comply or explain', the board refers to the possibility of explaining about alternative solutions. Alternatives or derogations are often justified with a reference to the Swedish company model. The analysis is statistical and does not mention individual companies but, instead, contains relevant data, for example, on the frequency with which auditors review the corporate governance statements. Every second year, the board's annual reports also contain a 'corporate governance barometer' that reflects opinions on corporate governance issues on the basis of a survey of the general public and of company leaders and investors, sometimes illustrating specific trends in their perception of corporate governance practices or proposals.

113. The board's annual report also publishes opinions on a wide range of company policy issues, e.g. dealing with the recent EU Commission proposals, on auditor appointment (by the state), rotation, independent directors, etc. According to the relevant statement, the board confirmed that it had given a negative submission to the Commission's consultation on corporate governance.

7.12. SWITZERLAND

114. Apart from the fairly elaborate provisions of the Companies Act, the Swiss corporate governance rules are based on two sets of provisions: the self-regulatory code elaborated by Economie suisse, the Swiss Federation of Business Association[144] and the instructions of the Swiss stock exchange[145], acting as a delegated body for the implementation of the listing and disclosure rules[146]. The corporate governance code, or 'recommendations', was originally drawn up in 2002 by an expert committee, and updated in 2007, with respect to remuneration matters, which is still the most elaborate section of the code[147]. The supporting associations are reported to have a wide freedom to emphasise specific aspects or depart from the code where necessary. At the level of these associations, the code does not refer to the 'comply or explain' approach.

115. The main instrument of the Exchange for regulating the issuers' activity are the Listing Rules[148], which form the basis of the different disclosure obligations to which listed companies are subject. The exchange, especially its listing department called 'Swiss Exchange Regulation' , acts as

144. Among these the Bankers' Association, the Institute of Certified Accountants and Tax Consultants, the Insurance Association, the chemical industry

145. This analysis relates to SIX, the Zurich exchange; there is also an exchange in Berne, specialising in SMEs.

146. Based on Art. 8 of the Federal Act on Stock Exchanges and Securities Trading (SESTA), the Regulatory Board shall decide on the admission of equity securities to trading in the SIX Swiss Exchange-Sponsored Segment and shall supervise compliance with the requirements of these rules during the process of admission to trading

147. The latest version to date: "Swiss Code of Best Practice for Corporate Governance", 2007, available at www.economiesuisse.ch.

148. www.six-exchange-regulation.com/admission_manual/03_01-LR_en.pdf, adopted on the basis of Art. 8 of SESTA. Other bodies of rules also play a role in corporate governance matters, such as the Directive on Ad hoc Publicity and the Directive on Disclosure of Management Transactions.

an 'independent regulatory body', granting admission to the exchange and monitoring the implementation of the Rules within the framework of its duty to organise the market. The information is produced under the issuer's responsibility, and technically submitted to the exchange by the sponsoring securities dealer[149]. The said department is assisted by two expert panels, one dealing with the developments in the fields of company reporting, the other more particularly with the application of IFRS (the Financial Reporting Expert Advisory Panel and the Specialist Pool for IFRS Issues)[150].

116. The listing Rules (art. 49), contain a reference to the Directive on Corporate Governance[151], a statement drawn up by the Exchange's listing department. In its annex the directive contains a list of disclosure items that must be included in the annual report, and this on a 'comply or explain' basis, requiring companies to disclose their business practices or to explain where they depart from the code. In the case of non- compliance, information will have to contain 'an individual, substantiated justification for each instance of such non-disclosure'. Particular attention is paid to remuneration issues, and to the presentation of the structure of ownership. Strikingly, the directive contains no explicit reference to the Recommendations of Economie suisse[152] as it deals only with the disclosure requirements, while the substance is left to the latter's code of conduct on the basis of a division of tasks agreed in 2002 (Kunz 2010).

117. As part of its overall duty to ensure adequate information to the market, the listing department of the Swiss Stock Exchange plays a significant role in ensuring compliance of the disclosure provisions. It examines annual reports, mostly by random-sampling, and comments on a number of specific items153. Following this review. each issuer will receive a comment letter, unless a preliminary investigation is required. The exchange regularly publishes statements about the investigations and about breaches of the rules, mentioning the name of the company involved and the nature of the violation. It may address reprimands to the company and also impose fines for breaches[154]. The sanctions are imposed by an internal Sanction Commission, deciding on a proposal from the Listing and Enforcement department[155]. The financial supervisor, FINMA, is obviously not involved in securing compliance with the listing requirements or the directive, except in cases of price manipulation.

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149. See Rules for the Admission of Equity Securities to Trading in the SIX Exchange-Sponsored Segment, www.six-exchange-regulation.com/admission_manual/05_01-RSS_en.pdf; art. 24 stated that:' 'These Rules were approved by FINMA, the Federal Financial Market Supervisory Authority on 23 April 2009 and enter into force on 1 July 2009.'

150. www.six-swiss-exchange.com/media_releases/online/media_release_201012081530_en.pdf.

151. Directive on Information relating to Corporate Governance (Directive on Corporate Governance, DCG), 29 Oct. 2008, www.six-exchange-regulation.com/admission_ma- nual/06_15-DCG/en/index.html.

152. This and the initial report are only mentioned among the other sources of information.

153. www.six-exchange-regulation.com/admission_manual/09_04_03-SER201103_en.pdf.

154. Article 61, 1 of the listing rules provides for the following instruments: the reprimand: a fine of up to CHF 1m (for negligence) or CHF 10m (if deliberate); suspension of trading: delisting or reallocation to a different regulatory standard: exclusion from further listings: withdrawal of recognition. For applications, see Bergbahnen Engelberg-Trübsee-Titlis AG, where a fine was imposed for not informing the exchange about management transactions; or, SIX Swiss Exchange fines Altin Ltd, a fine for breaching the ad hoc disclosure obligations of the DCG (26 January 2012; fine of CHF 100,000); investigation against Dufry Ltd of 19 January 2012, for not disclosing management transactions

155. See art. 9, 'Sesta' Federal Act on Stock Exchanges and Securities Trading, 24 March 1995; see for further details, Luechinger, S., Updates on Issuer Regulation, SIX Exchange Regulation, 24 November 2011.

118. Shareholder associations are also active, for example, in ESG[156].

7.13. UNITED KINGDOM

119. The UK Governance Code in its version of June 2010 is the successor of several other leading self-regulatory instruments[157] that have shaped governance in the UK and in many other countries. The code is widely followed by listed companies of all sizes. It is applicable to the companies with a UK Premium158 listing of equity shares, whether they have been incorporated in the UK or abroad. The rules of the UK Listing Authority, part of the Financial Services Authority (FSA), requires the application of the code, in addition to several other more detailed disclosure provisions[159].

120. In July 2010, in light of the diminishing position of UK institutional investors as shareholders in UK companies[160], a 'Stewardship Code' was adopted. The code states that it 'aims to enhance the quality of engagement between institutional investors and companies to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities by setting out good practice on engagement with investee companies'. This code is principally applicable to the managers of assets for institutional investors and more generally to all institutional investors[161], whether UK domiciled or not. These parties should indicate whether they have subscribed to this code and the FRC will subsequently publish the list of the subscribers (Cronin and Mellor 2011)[162].

121. Both codes – Corporate Governance and Stewardship – are supported by the FSA and based on a 'comply or explain' approach. Although covering different fields, there is likely to be substantive interaction.

122. The Corporate Governance Code contains five main principles that are mandatory[163], and forty-eight more detailed provisions that are based on 'comply or explain'. The overall implementation of the Governance Code is monitored by the FRC, which publishes overviews on the state of application, and the progress made, also giving indications on objectives and policies. Specific topics like gender diversity, the use of voting agencies and director rotation received special attention in the

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156. ACTARES, AktionärInnen für nachhaltiges Wirtschaften, Schweiz.

157. The Combined Code was the immediate predecessor; the original 1992 Cadbury Code stood as a model for most of the European governance codes.

158. This is the superequivalent regime under the listing rules, whereby conditions above the EU Listing Directive (or the standard regime) apply.

159. See fsahandbook.info/FSA/html/handbook/LR/9/8, § LR 9.8.6, sub. 5.

160. See p. 9 of the FRC Developments on Corporate Governance 2011 announcing a study identifying ownership of UK companies' shares. On their holding in overseas companies, but then on a 'best efforts basis': see introduction to the code.

161. At the end of 2011, there were 234 signatories, among which were 175 asset managers, 48 asset owners (mainly pension schemes and investment trusts, of which many (31) defined benefit schemes) and 12 service providers: FRC Developments on Corporate Governance 2011, p. 20.

162. See also Financial Reporting Council, The UK Stewardship Code, July 2010.

163. Leadership, effectiveness, accountability, remuneration, relations with shareholders.

2010 FRC overview. Full compliance is reported to have reached 50 per cent for the FTSE 350 companies, while 90 per cent comply with all but one or two of the provisions. Smaller companies also comply at similar rates[164]. The FRC also publishes guidance, for example on Board Effectiveness, or on Audit Committees[165]. A specialised panel within the FRC, the Financial Reporting Review Panel (FRRP) on complaint, screens, the reporting by individual companies and publishes its decision, but not its analysis[166]. A newly created Financial Reporting Lab will provide the opportunity for companies and investors to confront their ideas and develop new reporting formats.

123. Commercial organisations publish in-depth investigations with critical comments, but always on a no-name basis[167].

124. Arcot and Bruno (2006) investigated corporate governance disclosures for the period 1998–2004 and found that on the one hand companies did not make very frequent use of explanations, and rather, were inclined to box ticking, the relatively frequent absence of explanations (17 per cent) being considered a signal of the disregard by shareholders of the corporate governance matters. They also remarked that the quality of the explanations was generally weak, and often remained the same over the years. However, companies that did not publish explanations were the ones that most considerably improved, once they decided to comply.

125. The Stewardship Code, although also voluntary, is a different instrument, being addressed to a different audience, with different obligations. Up to now, the FRC has mainly launched a campaign for moving parties to sign the code, the FSA having declared it mandatory in the sense that 'managers should be required to disclose their commitment to the Stewardship Code'[168]. Signatories are expected to disclose, apart from their commitment to the code, the way they have applied its principles, and otherwise explain how they have taken the code's obligations into account. In its first report on the matter, the FRC identified four areas where disclosure should be improved: conflicts of interest, strategy for collective action, proxy voting agencies and accessibility to the stewardship statements. If, in principle, the approach seems to be similar to the one followed for the Governance Code, at the time of writing, it is still too early to analyse the actual implementation and enforcement in more detail.

126. Individual FRC action against companies failing to implement the Governance Code – or any of the other codes under the authority of the FRC – has not been practised to date. However, there are some indications that the FRC may consider engaging more actively with deficient practice, and that

164. See the Figures, p.11, FRC 2011, drawn from a Grant Thornton Study, www.grant-thornton.co.uk/pdf/Corporate_Governance_Review_2011.pdf and Manifest Total Remuneration Survey 2011.

165. March 2011.

166. Statement by the Financial Reporting Review Panel in respect of the report and accounts of Rio Tinto Plc, 15 March 2011, where it was analysed whether the annual report contained 'a fair review of the company's business and that the review required is a balanced and comprehensive analysis of the development and performance of the company's business'.

167. A Grant Thornton Study (www.grant-thornton.co.uk/pdf/Corporate_Governance_ Review_2011.pdf); see also Heidrick and Struggles, European Corporate Governance Report 2011, Challenging Board Performance.

168. See Handbook Notice, www.fsa.gov.uk/pubs/handbook/hb_notice104.pdf asset (FSA2010/57).

after having received a complaint about an individual company, may consider engaging with that company[169].

127. Several of the UK documents plead for maintenance of the self-regulatory nature of these codes, reflecting some fear that 'Brussels' would impinge on this field.

128. Finally, to date there has been no judicial case law dealing with the issue of codes on corporate governance. With respect to the legal status of the code and its enforceability at law, one can only refer to an old case relating to the Takeover Code, another self-regulatory instrument. The court declared itself very reluctant to intervene on the substance of the regulation[170].

8. PRELIMINARY FINDINGS

129. The overview of the different ways the national codes of conduct in the field of corporate governance are being implemented and monitored should now be compared and evaluated on the background in which they operate. This analysis may allow us to identify some general trends and offer an insight in the way these corporate governance rules could be made more effective.

8.1. THE PUBLIC OR PRIVATE CHARACTER OF THE CODES

130. In many jurisdictions the Corporate Governance codes are essentially developed by the business firms and their associations. In some cases there is no input from the public authorities or institutions, while in others the input is very limited and takes the form of limited participation in the standard-setting body, or support in the standard-setting process. Difficult to establish is the informal nodding by the public institutions relating to the self-regulatory process, or their influence on the appointment of members of the standard-setting body. Many codes are private, but have an inkling of public interest, and therefore are not indifferent to the public authorities that consider them as an alternative to public regulation.

131. At the other end of the spectrum are the codes developed by the securities regulator, as is the case in Portugal and Spain, where the standard setting is ultimately the work of the regulator, while implementation is followed up and verified by the regulator as part of its monitoring of the disclosure in

169. See FRPP Annual Report 2011, pp. 11–12. 'In such circumstance, however, it would need to be made clear that the judgment whether the governance arrangements adopted by the company (as opposed to the description of those arrangements) were satisfactory remained a matter for shareholders, not the Panel.' See also FRC reform consultation § 5.9, 'The intention would be to undertake supervisory inquiries to provide an under- standing of the reasons for the collapse or near collapse of a public interest entity or other issue affecting confidence in corporate governance and reporting.'

170. See R v. Panel on Takeovers and Mergers ex parte Datafin [1987] QB 815.

the annual report. In some cases administrative sanctions for violation of the code would be applicable, but obviously are rarely imposed.

132. Between these two alternatives are several more nuanced forms. In the UK the code is adopted by the FRC, a public sector regulator and followed up by one of its subcommittees. But the code reflects strongly the private sector mind and is the product of an extensive dialogue and consultation of the private sector. Also, no enforcement or sanctioning action has been undertaken, at least specifically on the basis of code provisions. A different balance is found in France, where the AMF plays a very visible role in the corporate governance debate and publishes a report on the application of the code, although the latter is self- regulatory.

8.2. THE DOUBLE-LAYERED SYSTEM

133. In a few jurisdictions, one sees an emerging trend to develop two layers of recommendations, or codes: one addressed to the boards of listed companies, and another addressed to their shareholders, especially the institutional investors. As both levels are complementary, this approach may lead to a more consolidated view of the developments relating to governance issues.

134. Traditionally, most corporate governance codes were addressed to the leaders of the companies and the issues they are confronted with: composition, role of the chairperson, committees, remuneration, relations with management, etc. More rare are the codes where the role and position of the shareholders are mentioned, and then only from the angle of the board and the way it should deal with them (e.g. UK, Belgium).

135. The role of the shareholders, especially the institutional investors, has recently been highlighted. Leading to the acknowledgement that their monitoring action may be the other moving force in the governance debate, authorities are increasingly relying on them, obliging them to vote, or to engage in stewardship. The effectiveness of this action is directly related to the structure of company ownership.

136. In countries where most of the publicly traded companies are dominated by blockholders, or controlling shareholders, the corporate governance provisions usually reflect this reality. The way in which these companies adapt to the corporate governance provisions is generally very high (i.e. in the upper 90 per cents). The effectiveness of the code is due to the acceptance by the directors – and usually also by the shareholders – of the importance to be seen as adhering to the code, as its provisions will generally not be in contradiction with their views. One should also mention the role of the press, public opinion, and the political world, especially as a consequence of their threat to adopt hard law. All of these factors lead to high levels of acceptance of the main provisions of the code. But on points that may potentially be contrary to these shareholders' interests, e.g. remuneration, anti-takeover protection, or derogations from preferential subscription rights, codes would be rather timid, if not silent.

137. This analysis is different with respect to countries where companies are mainly characterised by dispersed share ownership, where the weak- ness of collective action tools leads to negatively affecting the monitoring role of shareholders on the boards. These companies are more exposed to activist investors, building up significant stakes and putting pressure on the board, sometimes leading to full takeovers. In these countries, institutional investors have organised themselves to weigh on companies' decisions (UK, Netherlands). Comparable, but different, is the action deployed by investor protection associations (Netherlands, Denmark). Third, in a separate class, are the attempts to mobilise the asset

managers to engage more actively with the companies in their portfolios (UK, France). The action of these different groups of investors not only addresses corporate governance issues, but views the entire range of issues relating to the investee companies.

138. In studying the effectiveness of corporate governance codes, one should also take into account this second layer of action, which is usually not integrated in the codes, as the latter are mainly addressed to the board and management. Different approaches will be commented on later.

8.3. COMPLY OR EXPLAIN

139. Most of the self-regulatory codes discussed in the present Chapter are based on a 'comply or explain' methodology, meaning that though they may contain some binding principles, most of their recommendations are not binding on substance, but allow the addressee to choose another approach, in which case companies must provide appropriate explanations[171]. This does not mean that these codes are non-binding: the national provisions adopted in implementation of CRD IV state that listed companies must designate a code that they declare applicable to them ('adoption of a code'). But pursuant to these provisions, the application of the code is left to the company's freedom. This freedom is variable, as most codes contain different classes of provisions, some of which are binding under the comply or explain regime, others are not binding in the sense that companies may, but are not obliged to deal with them, or do not have to state their reasons for not applying these provisions.

140. The notion of 'comply or explain' is somewhat ambiguous and has stirred some debate with respect to its place in the overall legal system (Poulle 2008; Couret 2010). According to some, companies that comply do not have to give any explanation, thereby avoiding any risk of possible deficiencies in the explanations, and the liability that may be attached. They consider that only in the case of non-compliance are explanations due. Another group states – rightly – that the rule is: 'explain if and how you comply and explain if you do not comply, why and what your alternative is'. Companies should state their understanding about their governance model, and explain why they have chosen a specific formula, which in their view may be better than any one proposed in a code. The ultimate purpose is to inform the markets about how the company is governed, and what its views are about the topics dealt with in the code. Too many companies consider this as a 'compliance' exercise, mainly by way of box ticking.

141. This technique leaves a great freedom to companies, and deliberately so: in several jurisdictions the opinion lives that the codes allow companies to structure their governance the way they see best, and would not curtail their freedom to look for other, more effective governance techniques. After all, pillars of today's governance as independent directors, non-executive chair- men, audit committees, lead directors, and so on, are due to governance practice, but later picked up by regulation. This large freedom constitutes one of the weaknesses of the code system: on the one hand it is very difficult to gauge precisely what conduct lies behind the words in the governance statement, and the degree of reliability of the statements; on the other, it is well known that some statements are far from perfect.

171. See Statement of the European Corporate Governance Forum on the comply-or-explain principle, 22 February 2006, available at htpp://ec.europa.eu/internal_market/company/docs/ecgforum/ecgf-comply-explain_en.pdf.

142. What is a ‘proper explanation’? The published reports frequently mention irrelevant, boilerplate explanations, carried over from year to year, practice that should certainly be refused as an ‘explanation’. Several jurisdictions have published guidelines about the appropriate character of an explanation (Belgium, Netherlands, UK). An explanation should be considered sufficient if it allows the normal reader to understand which way the company is dealing with the specific issue, and why it is doing so. Giving the rationale for the conduct, or how the derogatory consequences have been mitigated, are part of a valid explanation. Mere reference to tradition, to internal agreements, even to charter provisions, are not convincing. Temporary derogations should be identified as such, indicating the time period for which they will apply. The statistical data therefore have to be accepted with caution. But what about reliability of explanations? There have been cases of misleading explanations and some suspected to have been false. Only in a few jurisdictions is there any monitoring of the meaningfulness of the statements. The question has been raised as to who is responsible internally for the statement: does the board approve the statement, and what is the involvement of the chair? Or is all this left to the corporate secretary or an assistant as a necessary but not very meaningful exercise? In certain matters, how can the explanation (e.g. about internal processes) be verified by an external observer?

8.4. HOW TO MEASURE EFFECTIVENESS

143. The effective implementation of hard law provisions is very often not directly measurable and can only be determined by a detailed observation or analysis of the sanctioning regime. This is rarely undertaken in the traditional company law fields. On the contrary, regarding the implementation of the governance codes provisions in all jurisdictions compared, extensive statistical reports have been published, essentially illustrating a strong level of adoption of the code.

144. Measuring effectiveness is a difficult exercise: it can be undertaken on the basis of the disclosures, presupposing that these reflect reality. More ambitious is the verification in a survey of the opinion of the different business leaders involved. A third method is external monitoring, as is undertaken in Portugal and Spain on the basis of the quality of the disclosures. Each of these methods has it advantages, but also its shortcomings.

145. There are some questions with respect to these statistical data. Generally, they measure the overall adoption of the code (usually in the upper 90 per cents), however, the individual items usually obtain much lower scores. A large part of the detailed statement are not very controversial: they reflect usual practice, and are carried over from year to year. The statistics should focus on the other provisions, as there the implementation is much lower, as was repeatedly evidenced by the data about remuneration. It also appears that the statistical figures published by monitoring commissions are considerably more optimistic than those drawn up by investor associations, or even by regulators[172].

146. Specifically in Germany, von Werder and Bartz (2012) have investigated the effectiveness of the 90 recommendations of the German code on the basis of a survey with chairmen of the Vorstand and Aufsichtsrat. In their view the conclusions are more optimistic than one might have expected, but are still evidence of the weakness of the approach. They depict an overall Codexmood (‘Kodex Klima’) that is moderately positive in the eyes of the interviewed, but is clearly more negative on specific points such as the cooperation between the Vorstand and the Aufsichtsrat. Their effectiveness analysis

172. See the VEB Effect, 2009, nr. 26 42, nt. 4; cf. Portugal, nt.137.

is based on internal information, leading one to wonder how investors can assess governance on the basis of the statements in the governance reports.

8.5. THE CODES VERSUS HARD LAW

147. In all jurisdictions compared there is, of course, a more-or-less detailed set of hard law rules applicable to companies on the basis of the Companies Act, accompanied by more-or-less elaborate rules stemming from financial regulation. Corporate governance rules supplement these legal provisions in the fields that are difficult to capture in hard, legally sanctioned regulations, where no ready made solutions should apply. This function is undoubtedly useful, more so as it allows for sufficient freedom for companies to frame their own organisation and conduct rules, flexibility that is more limited in law-based, even default rules. It also strengthens the sense of ownership and responsibility of boards for their own governance organisation.

148. The competition between the two sets of provisions is mentioned several times in the national reports, but no further analysis is made. This menace of a takeover of the soft law rules may be attributed to the lack of implementation of the corporate governance principles or provisions, the too general character of some of these principles, making public authorities distrustful of the outcomes, and at least for some of them, the bias in favour of the company leaders' positions. The process of 'juridification' is especially visible in fields characterised by strong controversy (remuneration, gender diversity) or slow progress (audit committees). The proposed CRD IV contains elaborate corporate governance provisions for credit institutions, where the traditional voluntary provisions are considered to have been too weak in light of the financial crisis. In the future these provisions will become binding legal rules, from which no derogation will be allowed, leading to quite an important change in the system (Barret 2012; Winter 2012a). Here, too, the informal, soft law-based action – often with the support of the supervisors – has obviously not been considered sufficient to avoid formal legislation to intervene.

149. In my view, the acceptance of the self-regulatory or soft law approach to corporate governance hinges on the development of a stronger system of monitoring and implementation and, if needed, some form of external enforcement. Stronger implementation and credible enforcement are essential to avoid corporate governance principles being further crystallised in formal state legislation.

8.6. DRAFTING THE CODES

150. Part of the credibility of the corporate governance codes depends on their draftsmen. In most jurisdictions, especially where the codes originated from the stock exchange area, leading business people took the initiative, while the drafting took place under their guidance by their assistants, usually with some flavour from academia, and in some cases, a link to the regulator as well. The ministries seem to have been involved in some cases, but this influence is difficult to assess due to its pluriformity. In any case, the codes mainly reflect the concerns of the business leaders, and as a consequence essentially address the issues they are confronted with within boards, with the management and in their relations to shareholders or other stakeholders. This business bias probably may explain the reduced trust of the political world. However, the corporate governance codes should not be used as alternatives to

government regulation: they introduce additional guidance principally with respect to the internal functioning of companies, and cannot be used to pursue public interest policies.

151. Although presenting some distinct differences, the national codes by and large all reflect the same approach and express the same concerns. Originally the Cadbury Code 1992 stood as their model, but since then national diversity has taken hold. The drafting process has become more refined over time, with public consultations on the basis of a proposal or an exposure draft, feedback statements responding to the consultation, stating reasons for the adopted solutions. A cost–benefit analysis has rarely been found, and may sometimes be welcome. In practice, drafts- men usually take inspiration from the codes of the neighbouring states, and the experiences in other jurisdictions. But efforts could be under- taken to better familiarise draftsmen with these evolutions, including the case laws that have been rendered in other jurisdictions. Some coordinating action undertaken by the FRC deserves support.

152. Access to the codes is greatly facilitated by their posting on national websites and for the complete worldwide collection on the website of the European Corporate Governance Institute (ECGI).

8.7. OBSERVING THE ADOPTION AND THE APPLICATION OF THE CODE

153. 'Adoption' of the code is used here in the sense that companies acknowledge that a code is applicable. This usually also means that the company applies the code. In some jurisdictions (Denmark, Austria), no further statement is necessary if all provisions of the code are complied with. In others, the code calls for a description as to how the company complies with the different provisions of the code, including the provisions which it does not apply. This distinction is important in the description of the monitoring of the codes: some monitoring only addresses 'adoption', other includes 'application'.

154. The follow-up of the corporate governance codes takes different forms. In certain states, it is considered that both adoption and application is a matter for the shareholders and the markets. Hence no specific efforts are undertaken, although initiatives are mentioned to stir interest for the corporate governance theme in general, and for the code in particular.

155. In most EU countries, there is a body – a commission or other body – systematically analysing the different corporate governance statements and registering the responses in a survey, mainly for statistical purposes. In this case it is the adoption that is measured. But as the analysis goes to the level of the individual provisions of the code, the survey yields some insight in the way companies deal with the different issues in the code.

156. This body is usually also in charge of the original drafting of the code; it will also follow up on the code's regular updating, whether pursuant to its original mandate or on a self-appointed basis. The identity of these observation bodies – here referred to as 'governance commissions' differs considerably: in several states, these 'corporate governance commissions' are the reflection of the draftsmen of the codes and therefore originate mostly from the local business circles or the stock exchanges. In others the distance from the business world is greater, and some members are selected from academia, or even from the public bodies, including ministries (Austria). The latter may also have a say in the appointment of the members of these bodies (Netherlands, Germany). Even in these cases, the codes remain essentially a self-regulatory instrument, but with external monitoring as to adoption.

157. Intermediate cases are frequently found: the public sector securities regulator may be actively involved, whether by publicly taking a position on the way the code is being implemented, suggesting

initiatives for improving the content of the disclosures, defining what is a 'proper explanation', or even offering interpretation of the code. In these cases, there is a subtle transition from a purely self-regulatory instruments, to an intermediate form going in the direction of regulation.

158. The UK position is special: the corporate code is part of the codes and standards adopted by the FRC, 'an independent regulator responsible for promoting high quality corporate governance and reporting to foster investment'. The FRC is not a government body in the traditional sense of the word, but accomplishes tasks of public interest, some of which have been delegated on the basis of different pieces of legislation.

159. At the other end of the spectrum, one finds the Portuguese and Spanish models, where the codes are 'self-regulatory' by name, but have been drawn up by or in close coordination with the securities commission, and are verified by the latter on the basis that the governance statements are part of the public disclosure made by listed companies and hence subject to verification like any other public information. These national bodies are more strongly involved in the application of the code, analysing in depth the significance of the explanations given. There adoptions of the codes is mostly active in surveys, whether undertaken by the governance commissions, by independent third parties (academics, accounting firms), by the securities commissions, whether alongside their action on applications (Portugal, Spain)[173] or not (Belgium, to some extent France).

160. There is no general tradition for the governance commissions to deal with the application of the codes and verify the quality of the disclosures and of the explanations, as distinct from the formal implementation. Although references are made to this type of more intrusive monitoring, few are the states where it is effectively undertaken. It would imply at least that the governance commission is able to address itself to the company's top bodies and analyse the motives for not applying the codes' provisions. The absence of an appropriate monitoring technique and investigative powers may explain why most monitoring is limited to statistical observations and general analysis.

161. This alternative approach, however, is pursued in some jurisdictions, most prominently in Spain and Portugal, where corporate governance statements are actively analysed and negative findings discussed with the company. A similar type of monitoring is found is Switzerland. Changes in the disclosures are requested, and in the case of refusal would give rise to disciplinary action. It would seem that the UK is also considering a change in that direction.

162. By way of conclusion, the European jurisdictions compared present a wide scale of answers to the question how the corporate governance code's implementation can be monitored. These differences reflect fundamentally different legal traditions, and different business and political environments. Therefore it will be difficult, if not impossible to prescribe a single pattern for the implementation of the code through- out the EU. This does not prevent some minimum level of monitoring being pursued.

173. Where the verification has been internalised in the securities regulator.

8.8. DISCLOSING NAMES

163. If the implementation of a corporate governance code has been insufficient, one might expect the monitoring commission, after having respected due process and discussed the matter with the appropriate bodies within the company, to disclose the names of the companies that have resisted its recommendations. This would warn the markets about deviations from the code, and also work to shame the unwilling company ('name and shame').

164. This is not the usual approach of the monitoring bodies. One presumes that legal reasons – the rules on libel and slander – prevent them from being outspoken about the kind of violation, and the identity of the perpetrator. Moreover, the process of establishing breaches of the code would also have to be clearly worked out, as publication will legally be considered a sanction in some jurisdictions at least, triggering human rights concerns. Public authorities would be reluctant to engage in this type of action, as the code is a private statement that should not be enforced by government action, unless authorised by the legislator. Private bodies would not easily be mandated to engage in such disciplinary action, although the listing conditions may confer this kind of powers (Switzerland, Luxembourg, Sweden, Denmark).

165. This modesty is not shared by the investor associations: the French asset managers' association, the AFG, publishes its 'alerts' by referring to the agenda of the identified AGM and the items it criticises. The Dutch association of institutional investors, Eumedion, screens the AGMs with reference to the individual companies[174]. In the Portuguese practice, companies are mentioned by name, indicating, for example, their position in the compliance scale. When action is undertaken, the outcome of it is not, however, always mentioned. This is, of course, different from the usually high-profile legal actions at the initiative of investor associations (especially in the Netherlands, France, and some in Germany as well).

166. Based on techniques for comparing the quality of consumer products, or financial services, one could also consider the publication of data about critical governance points. This is attempted in the Netherlands, where the VEB website contains data about the remuneration paid to the CEOs of major Dutch firms[175].

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174. See e.g. www.eumedion.nl/nl/public/kennisbank/ava-evaluaties/2011_ava_evaluatie. pdf; see also the VEB Annual Report 2010, p. 13, according to which the Corporate Governance Commission intends to name companies in breach of the code. VEB itself publishes a list of purportedly independent directors that in its analysis are dependent; see *ibid.*, p. 17.

175. On the website of VEB under the heading 'bestuursvoorzitter' with an indication of the increase/decrease for the last year, and data about options and bonuses.

8.9. THE GENERAL ROLE OF THE SHAREHOLDERS IN THE CODES' EFFECTIVENESS

167. The relatively recent involvement of the shareholders in corporate governance regulation is obviously very different in countries with concentrated ownership versus those where shareholdings are widely spread. However, one should warn against a simplistic view: in most European countries the two models coexist, the dispersed model often applying to the largest firms.

168. In companies with concentrated ownership, investors outside the controlling group do not usually play an important role. Attendance at the meeting by these investors is generally low, although institutionals, acting through voting agents, may have swollen the numbers in the last few years (Van der Elst 2012). The role the outside investors play is generally limited, illustrated by the low percentage of negative vote or abstentions[176], nonetheless they may weigh on the market price for the company's shares.

169. It is striking that, in both companies with concentrated and with dispersed ownership, it is usual practice for boards to strive for adherence and voluntary implementation of the corporate governance code, and to avoid damage to reputation for deficient policies in this respect. Both types of companies have been willing to make considerable progress in developing audit committees even before this was mandatory, to develop adequate risk models and explain their risk-management tools, and more recently to explain their business model and its viability. One might refer to these examples as some form of 'competition for excellence'. More sticky has been the issue of remuneration, where ultimately the legislator had to intervene (Lorsch and Simpson 2009)[177]. The same applies to board diversity.

170. Even in companies with concentrated ownership, this approach has supported the standing of the company's equity in the market, has gained praise for the management, and last but not least, has supported the market price of its equity to the benefit of both the blockholders and the investing public.

171. The relevance of the corporate governance codes and their effect on share price performance have been investigated by several European researchers (Gompers et al. 2003). The opinions are divided. Some papers draw attention to the need for stricter enforcement. Whether institutional investors effective influence general meetings is also doubted. The following papers can usefully be consulted in this context.

172. Clacher et al. 2008 see an exceptionally strong link between corporate governance in general and in performance, while MacNeil and Li Xiao (2006) conclude that there is a strong correlation between performance and non-compliance, meaning that shareholders of well-performing firms tolerate non-

176. It is well known that these investors only cast a negative vote if no other way of influencing the company's decision has been successful.

177. Although in a certain number of cases investors have been able to refuse a proposed remuneration plan: 'Shell shareholders revolt on pay', 19 May 2009, available at htpp://news.bbc.co.uk/2/hi/business/8058103.stm. Recently, the 'shareholder spring' has witnessed numerous cases of open criticism of remuneration, leading in some cases to reduction of the amount, or even the departure of the CEO as his remuneration increases notwithstanding the poor result of the company: 'Moss, A. Aviva CEO, Resigns.

compliance more easily. The conclusions of Shaukat and Padgett (2005) point in the same direction: compliance matters, not just as a box-ticking exercise, but as a trigger of real change in the governance of large listed companies, for which shareholders are willing to pay a premium. In Germany, some writers point to the beneficial role of corporate governance codes: Zimmermann et al. (2004) concluded that the degree of compliance with the code is value-relevant information, attributing this to capital market incentives (or pressures) that might lead to a broad adoption of the code's recommendations, even though the enforcement mechanisms connected to the code are relatively weak. Drobetz et al. (2003) analysed differences in firm-specific corporate governance and document a positive relationship between their Corporate Governance Rating and firm value. More critical voices are heard from Prigge (2010) pointing to limitations in the corporate governance empirical analysis, while the role of the corporate governance code is doubted in Nowak et al. (2006), who found that the code has little effect and state as one of their conclusions that 'further evidence to the hypothesis that self- regulatory corporate governance relying on mandatory disclosure with- out independent monitoring and legal enforcement are ineffective and do not positively influence shareholder value'. Van der Elst (2012) found that the increased presence of institutional investors did not materially affect the approval rates for the usual agenda items.

After Shareholder Revolt On Compensation', 19 May 2012, available at 2012 www.huffing-tonpost.com/2012/05/08/andrew-moss-aviva-ceo-resigns_n_1499209.html.

173. In the companies with dispersed ownership, the corporate governance rules have seen their full deployment. Institutional investors and hedge funds have often taken an activist stand to convince the general meeting of their point of view. In several cases battles were fought in public opinion and sometimes successfully in the courts as well, most recently and in some cases successfully, on the issue of compensation[178].

174. In companies with a large, dispersed ownership structure, institutional investors are usually fairly reluctant to undertake common action, out of fear of being held to additional obligations, especially those relating to 'concert action'[179] and to insider trading, or under the even stricter rules of the US regulation FD on Fair Disclosure. Therefore they usually prefer to remain passive, at most limiting themselves to the exercise of their voting rights in cases where voting is mandatory. Larger institutionals sometimes act individually and exercise pressure on the companies' governance (e.g. on appointments of directors and their remuneration) and on strategy. In at least three jurisdictions, i.e. France, the Netherlands and the UK, institutional investors publicly exercise considerable influence on listed companies, especially with respect to their governance. Methods are different: in the UK, an elaborate system, mainly based on the action of the asset managers, has been put in place in the Stewardship Code. In the Netherlands, a powerful association of institutional investors engages with the management, while smaller investors act directly through an investor protection association, or pursue their objectives with public, and sometimes legal action. In France, the two models are found, one being based on the asset managers, the other represented by investor protection defenders[180]. Some of this action is deployed in highly visible public statements, press interviews and legal action, while another part takes place in discreet contacts and discussions. The effectiveness of these

178. A prominent case is Storck, in which activist investors were able to rally a majority around their proposition to split up the company, to the dismay of public opinion and the press. See Court of Appeal Amsterdam (OK) 17 January 2007, LJN AZ6440, JOR 2007, 42 (Centaurus c.s /Storck).

179. Leading to additional disclosures under the Transparency Directive rules, or even to a mandatory bid if the bid threshold is crossed.

180. Colette Neuville, founder of ADAM (Association de de´fense des actionnaires minoritaires) is a well-known defender of shareholder rights in France.

approaches is difficult to measure, although the concern expressed in response to activist (hedge) funds indicates that boards and management of target companies are far from indifferent to the potential threat these investors represent to their position. However, it can safely be assumed that corporate governance ideas are effectively relayed through organised shareholders, whereby the invisible action – that has been mentioned for some jurisdictions – is difficult to document, as investors prefer not to influence the company's policies by acting in the general meeting or in public, which is considered a last resort. Normally, these large investors will discuss the company's policies including governance issues, with the boards or with the management, but would be more reluctant to engage with other investors out of fear of being held to the consequences of concerted action. The Stewardship Code in the UK is partly based on this assumption. Whether their opinion is taken into account often appears to be doubtful. Therefore, in some instances, more forceful action has been engaged: cases have been mentioned where several institutionals, acting within their professional organisation, exercised collective pressure to have a board member, or more likely a member of the management, discreetly removed. But these are rather exceptional cases and only known from hearsay. Further escalation of pressure takes place through public statements – or even leaks – in the general meeting and legal proceedings.

8.10. TOOLS FOR MORE EFFECTIVE MONITORING BY SHAREHOLDERS

175. The first main avenue to strengthen implementation of good governance lies with the internal forces within the companies themselves, i.e. their boards, especially the independent directors, shareholders and external auditors (Weir et al. 2001). The board is the first in line to ensure good governance, and should organise itself by attracting the necessary expertise, create internal governance rules and procedures, institute governance committees, proceed to self-assessment and board evaluation, externally if needed. The applicable laws have sharpened their role in terms of liability[181].

176. The auditors play a useful role in verifying the data as reflected in the internal accounts, e.g. on remuneration (Hommelhoff and Mattheus 2003; Wohlmannstetter 2011). These different players could be called 'internal' monitors, as opposed to the 'external' ones to be discussed below.

8.10.1. Making room for a more continuous dialogue

177. The shareholders are the ultimate beneficiaries of the corporate governance efforts undertaken by the companies and all other parties involved, but the dialogue with them is often weak. Code provisions are adopted without much consultation[182], and in companies the dialogue is limited to casting one vote a year, usually through a voting agent.

178. Companies interact with shareholders once a year at the general meeting: in many jurisdictions the AGM is usually a rather dull, ritual, although recent experiences with 'say on pay' may point to a

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181. The legal liability of supervisory directors of German financial institutions (Aufsichtsrat) has been sharpened by shifting the burden of proof to the directors and extending the liability limitation period for listed credit institutions: 'Gesetz zur Restrukturierung und geordneten Abwicklung von Kreditinstituten, zur Errichtung eines Restrukturierungsfonds für Kreditinstitute und zur Verlängerung der Verjährungsfrist der aktienrechtlichen Organhaftung' (Restrukturierungsgesetz, RStruktG).

182. See the German change of position in Von Werder and Bartz (2012), nt. 192.

reversal. In other companies – well known in Germany – the AGM offers the scene for the public expression of a very wide range of feelings and frustrations, to the point that governance recommendations had to be adopted to limit their length[183]. What are the signals the companies receive from their investors and how are these transmitted? In companies with concentrated ownership, the blockholder will indicate his views, leading other shareholders to stand more or less aloof. From the company side, signals are limited to the price evolution in the markets, and perhaps the visit of one or two engaging shareholders. These are politely listened to, or are received by the investor relations department. There would be little real engagement, even less a sense of partnership. Companies should be obliged to develop effective engagement procedures.

179. The essential elements would be that shareholders and investors should be able to expose their concerns to the company management, while the latter would be obliged to organise the necessary procedures for allowing this dialogue. Such dialogue would contribute to avoiding excesses or abrupt positions at the AGM, while withholding activist investors from undertaking ill-informed actions. There are several means for companies to open this more continuous dialogue, for example, by the use of electronic means. This would modify the agency relationship, interested shareholders being able to express their opinion on a well-informed basis, and management having a feeling about investor sentiment. The voting process as such would be the crystallisation of the relationship, not its exclusive and unique expression. It would also modify the role of the voting agencies, as they would have to take into account the outcome of this dialogue of which they can be an active part. Although this subject goes beyond the limits of traditional corporate governance concerns, one might explore to what extent the objective could be included in the companies' charter and further organised on the basis of soft law standards.

8.10.2. Organising the role of institutional investors

180. Among the different classes of shareholders, the institutional investors already play a prime role in the monitoring of governance and one should further explore how this role can be made more effective. The obligation to vote and report how the votes have been cast may be the least bad solution, but is not a very convincing instrument, as institutionals will merely implement it without being really interested in or even aware of how the votes have been cast. On the other hand, one cannot expect institutionals or asset managers to follow up on each of the thousands of companies in their portfolio. Feasibility and cost are the issues here (Van der Elst and Vermeulen 2011)[184]. Selective but active engagement with investee companies seems a better alternative, provided the necessary guarantees are introduced as to the negative consequences of this engagement, mainly with respect to obtaining price-sensitive information that leads to block trading or the application of the rules on concerted action. Solutions may be found in internal procedures, similar to the Chinese walls that have been adopted in investment firms.

181. The voting activity of institutional investors cannot be assessed with- out considering the role of voting agents[185]. For institutional investors that hold hundreds, and in some cases, even thousands of lines of equity investments, exercising their voting rights, as is now mandated in some legislation, is

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183. See for Germany, where the Kodex recommends that a general meeting should not last more than 4-to-6 hours (§ 2.2.4).

184. The authors see several cost elements that should be taken into account: (1) conven- tionalism/micro-management, (2) management distraction, (3) risk aversion, and (4) lack of transparency.

185. See the ESMA consultation 'An Overview of the Proxy Advisory Industry. Considerations on Possible Policy Options', 22 March 2012; Fleischer (2011), propos- ing to put proxy advisers under supervisory 'Kuratel', at 173.

practically impossible, particularly as most general meetings take place within a timespan of about two months. In that sense, voting agents offer an efficient solution to this challenge. However, the intrinsic quality of this type of engagement should be questioned, as the investor usually will not be able to make an individual determination about how the vote should be cast taking into account the specific circumstances of each investee. As a consequence, it will be the agent determining how the principal will vote, based on the model schemes that the voting agencies have developed. The argument that voting agents discuss with their principals the way votes have to be cast seems unlikely, due to the very considerable number of investees for which votes have to be cast. By relying on the uniform voting instructions, voting agencies acting for several institutionals amplify their impact, increasing the risk of biased, or unfounded positions. Therefore, one may wonder whether considered individualised voting should not be preferred.

182. A more solid approach might be found in allowing institutionals – or asset managers as their agents – to set up an entity[186], separate and independent from their main portfolio, in which some shares could be lodged of those companies in which stronger involvement would be planned. This separate entity could act as the engaging shareholder, with a clear mission to follow up on the affairs of the investee. The entity would be forbidden from trading in the portfolio, which would eliminate the conflicts of interest, and provided the legal prohibition on passing inside information is adapted, most of the insider trading issue could be eliminated. There should be an appropriate Chinese wall with the main portfolio. Most importantly, there should be no confusion in terms of objectives between the main portfolio and the separate entity. The latter would be provided with a clear separate governance, and a clear budget, on which the participants in the main portfolio would have to decide. The present confusion about who pays for governance activism would be eliminated.

8.10.3. Engagement and stewardship

183. How significant shareholders construe their relationship with the investee companies presents a great individual diversity which is due not only to differences in the percentages held – what is fairly obvious – but also to the organisation of the controlling blocks and differences in the legal and social environment in which these blocks are held. The usual differentiation between companies with concentrated or dispersed ownerships should be kept in mind. Companies with concentrated ownership have widely adhered to the corporate governance codes, although these may have restricted the influence of their controlling shareholders. In companies with dispersed ownership, the governance matter is essentially in the hands of the board, with little influence from the shareholders and serves to rebalance the influence of the management. It is essentially with the dispersed companies in mind that the proposals about engagement and stewardship of the dispersed shareholders have been developed; however, they deserve some further analysis in both types of companies.

184. Winter (2012b) has recently proposed a three-layered form of involvement by dispersed shareholders, which he called compliance, intervention and engagement. He considers that much of the involvement of institutional investors is in fact compliance with the applicable code or instructions, by having adopted a mandatory voting policy leading to thoughtless but mandatory exercise of voting rights, and entrusting a voting agency with making the choices and casting the votes. As most institutions have such large diversified portfolios, this is the only type of involvement these investors can effectively practice. Intervention hap- pens when shareholders enter into a dialogue with the management to make it adjust its strategy or policy, often in order to increase share- holder value or to support ESG objectives. The intervention of activist shareholders belongs to this category, being characterised by the fact that their action is usually a one-off. The third group, stewardship, refers to the

186. Company, trust, foundation.

longer-term perspective of the engagement and the intention of the investor to build a structural relationship. Therefore it presupposes a long-term ownership, which is mostly incompatible with the regulation applicable to some of these investors (particularly investment funds, held to honour daily withdrawals). The relationship of these shareholders bears some resemblance to that of the controlling shareholder, but necessarily remains more high level, due to weak incentives and being handicapped by the rules limiting access to confidential or price- sensitive information and by the absence of effective instruments to bend the company's conduct. In the past, their action was limited to recommendations or some often-discreet pressure, leading in a few cases to changes in the board or in the management team. If they are able to mobilise a sufficient number of shareholders behind their plan[187], these institutionals may be able to trigger a bigger change, as has been illustrated by recent cases on 'say on pay'. Decisions are than supported by a vote in the AGM and reflect a long-term interest in the company, which is quite different from the actions undertaken by activist investment funds who pursue short-term gains.

185. With respect to companies with concentrated ownership, the influence of the shareholders is more complex, covering a wide variety of situations, with shareholders holding more than half of the votes, others with a factual majority, while further down the majority may be based on the alliance of a series of smaller blockholders. Control will often also be based on control-enhancing mechanisms, among which the pyramids occupy a central position. In front of this diversity, the way the views of the control block is transmitted to the company will also vary significantly: in the case of a majority owner, the company will likely be informed about the owner's view and at least will have sufficient regard to it. The other types of controlling shareholders are likely to use more indirect means, or safeguard support from other investors by following policies agreeable to them (e.g. generous dividend distributions). Common to all of these cases is that controlling power is usually asserted by the possibility that the shareholder dictating or at least influencing the appointment of himself or a number of allies on the board, but would generally not extend to all decisions taken by the board. These share- holders would normally only decide on significant aspects of company life, especially the decisions that directly affect them, such as dividend distributions, diluting share issues, changes of the articles of incorporation, business restructuring and, especially, mergers. Key appointments, such as chairman and CEO, would also be at least pre-approved.

186. The possibility to practice 'intervention' by non-controlling shareholders will depend on the coherence of the control block, but remains possible even in non-majority-controlled companies. But even in fully controlled companies, minority shareholders may claim for abuse of majority powers which in some jurisdictions many lead to far-reaching remedies. Activist shareholders have been able to mobilise the public investors and impose drastic changes even in companies with blockholders[188]. In order to counter these attacks, companies have an interest in presenting themselves as applying 'good governance', which will effectively be achieved by pointing to the strict application of the governance code. The cited decisions of the Dutch Supreme Court could be an example in this direction.

187. Stewardship is a more universal notion and could be applied in all types of companies. It would, rather, function as a support to the incumbent board, but might conflict with the views of the controlling shareholders, e.g. on their long-term development views. Up to now there has been little experience with stewardship techniques in con- trolled companies, where the matter is usually dealt with by the investor relations department. Whether that will suffice in the future is question- able, and

187. Even not a majority, as boards will be reluctant to oppose a large minority of shareholders.

188. See the Storck case, nt. 209

boards may usefully look at better ways of communication. Direct relations with controlling shareholders may also have to be considered.

188. As to *compliance*, even if its overall effectiveness can be doubted, it might be worthwhile to restrict its mandatory use to specific items of the agenda of the general meeting where the investors have a more direct interest (e.g. anti-takeover devices).

8.11. EXTERNAL MONITORING BY THE CORPORATE GOVERNANCE COMMISSIONS

189. Several schemes have been developed to make the codes more effective, and the acceptance of these schemes will depend on the legal, social and political environment within which these codes have been adopted and implemented. It is reasonable to admit that no one solution will fit the whole European Union and beyond. Not only the content of the codes, but also the methods of implementation have to take account of local diversity, allowing for experimentation with a wide range of techniques, some of which have been illustrated in the country overview.

190. A number of external drivers in support of effectiveness will be mentioned only generally here, for lack of direct legal relevance. We would mention the quite important influence of the press, public opinion, the political world and the judiciary when they deal with code provisions or concepts. Their effectiveness varies depending on the individual issue (remuneration, gender diversity) and depends on the existence of an alert press and public opinion. We will instead focus on the structured external monitoring models, of which there are already several in place.

8.11.1. Nature and role of the corporate governance monitoring commissions

191. The strongest monitoring model is undoubtedly the Portuguese–Spanish one, where the securities supervisor adopts the rules, assesses their implementation and, if needed, takes enforcement action. In both cases it is based on the inclusion of governance statements in the annual reports to which the securities supervisors extend their oversight in the framework of the national legislation adopted pursuant to the implementation of the Transparency Directive[189]. It is argued that, as this legal basis applies throughout the Union, this supervisory regime should in fact be applicable in the entire Union. However, the argument only applies to a governance code that has a regulatory origin and when the information to be disclosed is founded on a statutory provision, even if the latter is of the 'comply or explain' nature. Therefore this model cannot easily be exported to other jurisdictions, where governance codes are the product of the private sector, where public authorities might not be very willing to spend their time and means for enforcing an instrument that originates outside the public sector and would oblige them to impose objectives that are difficult to achieve, having been laid down in a private instrument. In fact, the situation is more complex: in Belgium and France the securities supervisors undertake elaborate scanning of the governance practices, although the codes are undoubtedly of a private nature. However, these regulators remain on the sideline as far as non-regulatory standard setting and individual enforcement are concerned, as this would otherwise change the corporate governance dialogue from a private, self-regulatory intervention to regulatory action. On the other side,

189. Transparency Directive 2004/109 of 15 December 2004. See art 4(2)(b) and art. 24(4)(h), referring to the reporting framework. These provisions do not clearly oblige national supervisors to verify the information in the annual reports.

companies would strongly argue that a flexible, preferably self-regulatory corporate governance model, would best meet their needs. But it is undeniable that the trend goes in the other direction, and that an increasing number of governance tools are likely to become governed by official, or public regulation (e.g. on risk management, diversity[190]).

192. Most corporate governance monitoring commissions have a private law status, although with a varying degree of public involvement. These bodies are very effective in the standard-setting process and in raising awareness of governance issues. There is no particular call for adapting their composition in depth: states that prefer a private body should be able to continue to do so, similar to those relying on mixed formulas or on a securities regulator. By allowing for this freedom of choice, private companies will maintain ownership of the corporate governance project and ensure its development, taking account of changing business practices. The presence of experienced business leaders will avoid code provisions or decisions that might not reflect good business practice.

193. In some jurisdictions, no monitoring takes place: this is regrettable, and should be remedied. The status of the monitoring body can be left to national decision, with a certain preference for private bodies composed of experienced business leaders.

8.11.2. Monitoring tools

194. The external monitoring of actual governance practices essentially takes place using statistical tools. Although these are useful, more attention should be paid to the governance practices and explanations and to their meaningfulness. This could be pursued by addressing specific practices for all companies subject to the code, not in one particular, but across several jurisdictions. A topical comparative insight is a powerful instrument to identify weaknesses or recommend improvements, referring to those who have already adopted the better discipline. Said comparative action might lead to more de facto harmonisation and streamlining of the disclosures, and contribute to the enhancement of governance practices as a consequence of 'competition for excellence'. In the same vein, more attention should be paid to the experiences in other jurisdictions, not only with respect to the way the substantive issues are handled, but also as to the means used for ensuring more effective implementation of the codes.

195. The presumption that corporate governance reports reflect reality should be subject to regular verification. Whether the auditor should undertake this task – as is the case in some states – or whether it should be undertaken in a direct dialogue with the companies, is open to debate. But the knowledge that the disclosure may be subject to verification will contribute to better practices and more meaningful disclosure. A risk- based approach would be indicated here.

196. Corporate governance commissions should be able to engage with companies and their stakeholders on specific subjects, e.g. topics that are raised by investors that have been identified as outliers in the statistical exercise, or more generally have received public attention. The corporate governance commission should be entitled to interact with companies with respect to their implementation of the code provisions and to request explanations. In a high-level dialogue, the arguments for companies not applying certain provisions or not putting forward appropriate arguments for departing from the code, should at least be discussed. The discussion should not be bureaucratic or administrative, but directly engaged with persons experienced and knowledgeable in governance

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190. The trend can be noticed in several EU states: Italy: Law 120 'Gender Balance on the Boards of Listed Companies' of 12 August 2011; Belgian Law on diversity, Act on Gender Diversity L. 28 July 2011, nt. 22; and French act Loi relative à la représentation équilibrée des femmes et des hommes au sein des conseils d'administration et de surveillance et à l'égalité professionnelle, of 27 January 2011.

matters. On the other hand, companies should be obliged to respond to the invitation and to answer the questions posed by the monitoring commissions, particularly explaining the reasons for not adopting the commission's recommendations. But the last word remains with the company.

197. If the foregoing remained ineffective, as the ultima ratio the corporate governance commission should have the right to publish the company's name. In that case, it should be protected against legal action by the firm criticised, except in the case of gross or wilful negligence. The protection should extend to the rules on libel and slander. Before applying this instrument, due process must be followed. As to whether other sanctions should apply (such as civil liability or even professional disqualification), this is better left to the applicable legal system[191]. Said changes could be introduced on a soft law basis, especially through contractual instruments[192] or in the listing conditions. The legal protection for the monitoring commissions might require legislation. The concept of self-regulation and 'comply or explain' should be maintained, allowing for much desirable flexibility and avoiding petrification. At the same time, the outcome should be credible and contribute to healthier organisation and functioning of listed companies.

8.12. IS THERE A NEED FOR FURTHER HARMONISATION?

198. The issue of a Europe-wide harmonisation has been mentioned by several national governance bodies. There is generally little love lost on this idea. Therefore, it might be a valid alternative for governance commissions to explore more in depth what they can learn from each other and attempt to align their recommendations and move to more common concepts. At the same time, as has been presented before, the companies themselves could usefully strive to streamline their governance practices and disclosures. Voluntary initiatives based on a bottom- up approach could be undertaken by the Europe-wide business associations. This cooperative exercise has not been undertaken to date and one may call on the national governance commissions to take initiatives in this respect.

199. If none of these attempts were successful, it might be useful to develop a series of high-level principles against which all national governance codes could be measured, reflecting the common denominator among the best practices as laid down in the codes today, but leaving the national standard-setters free to adopt the principles or provisions that are best adapted to their legal order.

200. The large diversity of company ownership and, hence, of governance regimes in the EU, reflected in differences in the legal frameworks, are strong arguments for avoiding a uniform approach to corporate governance issues. This applies to both self-regulatory as well as legal interventions.

191. So, e.g., in the Dutch system disqualification would belong to the measures that can be ordered by the Enterprise Chamber (art. 2:356 Burgerlijk Wetboek).

192. Comparable to the code applicable to institutional investors in the UK.

9. RECOMMANDATIONS

201. The chapter has identified a number of fields where the present status of applying corporate governance principles could be improved. The following 10 recommendations are addressed to the national entities responsible for developing, adopting and applying corporate governance principles and codes and to the companies that apply these codes.

1. Corporate governance codes are useful instruments to deal with governance issues. Their credibility will depend on the effective application of the codes.

2. Comply or explain' is a sensible approach to corporate governance issues: 'comply' should be understood as obliging companies to extensively explain their governance model and related mechanisms. 'Explain' should lead to proper, meaningful explanations.

3. Companies should organise their contacts with investors on a more frequent and intensive basis than merely at the AGM.

4. Institutional investors and asset managers should organise themselves to be able more actively to engage with investee companies, avoiding restrictions in present regulations. The creation of a separate governance subsidiary with sufficient funding could usefully contribute to that objective.

5. Regulations on concerted action and on insider trading should not stand in the way of properly organised engagement efforts.

6. Companies should actively monitor their governance mechanism internally.

7. National corporate governance bodies should be installed in charge of following up on developing and monitoring the application of the codes. External monitoring should take place by senior and experienced business persons.

8. Cross-border contacts, including monitoring on a cross-border basis, can be a useful tool for developing a common benchmark on certain governance subjects.

9. These corporate governance bodies should be entitled to engage in an active dialogue with companies, allowing them to identify best practices, including with respect to the implementation of the codes

10. National corporate governance bodies should be entitled to pub- lish the names of companies with deficient corporate governance practices; protection against liability and libel and slander should provided for.

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