Corporate Governance and Company Law News (July 2009)

compiled by Johannes Heuschmid for SEEurope project (contact: mstollt@etui.org)

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European Private Company (SPE)

In the follow-up to the report on the European Private Company (SPE), adopted by the European Parliament in March, the Czech presidency issued a new Council proposal on the SPE. This proposal includes some improvements (for example, provisions dealing with the special negotiating body for worker involvement) but still has many shortcomings, and not only with regard to board-level participation rights.

Recently, the upcoming Swedish presidency has been working on a new proposal. It will probably be published around September 2009. From a trade union perspective, it is hoped that this proposal will improve the defects in the recent proposal. The core points for improvement should be: (i) a substantial cross-border element, (ii) obligatory provisions regulating the corporate governance structure adopted from the SE and (iii) a general clause on the duties of directors, which includes taking into account the interests of all stakeholders (especially employees) and the duty to conduct negotiations on worker involvement – which also includes issues of transnational information and consultation – in each case of founding an SPE (as is the case in the SE). As unanimity of the EU Council of Ministers is required it is not

likely that all EU Member States will agree to legislation which undermines well-established national standards.

Links:

- European Parliament report
- More information regarding the SPE
- ETUC position, press release

Commission activities in the face of the financial crisis: executive remuneration policies and regulation of alternative investors

Executive remuneration policies

In response to the financial crisis, in April 2009 the Commission launched several initiatives in the field of remuneration policies. Specifically, the Commission has adopted a Communication (COM (2009) 211 final) and two complementary Recommendations on remuneration policies (Recommendations C (2009) 3177 and C (2009) 3159). In addition, the Commission plans to address remuneration policy in banks and investment companies through a set of modifications of the Capital Requirements Directive, which will be proposed soon.

In the Communication accompanying the Recommendations, the Commission underlines that the financial crisis has exposed serious weaknesses in the way financial markets are regulated and supervised. Therefore, the Commission is planning a wide-ranging reform, drawing on lessons from the crisis and delivering stable and reliable financial markets for the future. The Commission Recommendations are the first stage in the Commission's strategy to address this issue. The objective is to improve risk management in financial firms and to align pay incentives with the sustainable performance of companies in general. It is planned to complement the Recommendations, in a second stage, with further legislative proposals to bring remuneration schemes into the scope of prudential oversight. However, the recent Commission initiatives appear inadequate, so far. A much more fundamental realignment of the policy measures taken by DG Market in recent years would be necessary, moving away from the shareholder value approach to a stakeholder approach. This would be more appropriate, as such an approach is rooted in most European company law regimes.

The first Recommendation (C (2009) 3177) adopted by the Commission deals with the regime for the remuneration of directors of listed companies and complements Recommendations 2004/913/EC and 2005/162/EC. The main objective is to align executive remuneration with companies' long-term interests. To achieve this, the Recommendation provides for a balance between long- and short-term performance

criteria; for the deferral of variable directors' remuneration; for a minimum vesting period for stock options and shares; and for the minimum holding of part of the shares until the end of employment. As a last resort, companies should reclaim variable components of remuneration that were paid on the basis of data which later proved to be manifestly misstated. It is unacceptable, however, that the Commission aims only to improve shareholders' oversight on remuneration policies, since shareholders in the recent crisis have proved that they, acting alone, are far from able to guarantee the long-term sustainability of a company. In fact, it would be necessary to strengthen the right of all stakeholders, including workers, to oversee management in the running of companies.

The second Recommendation (C (2009) 3159), on remuneration policies in the financial services sector, addresses the perverse incentives and excessive risk-taking which are rife in firms active in this area. The Recommendation puts the EU in the vanguard in implementing the commitments made at the G20 Summit in London on 2 April 2009.

Although the direction taken here with the Communication and two Recommendations can be seen as a positive first step, nevertheless the Recommendations lack the specificity needed to properly regulate executive remuneration. In particular, the use of stock options should be restricted since they are a mechanism which leads to greater risk-taking on the part of bank management. Proper regulation of executive pay needs to have clear quantitative rules for different components of management pay.

Links:

- Communication from the Commission: COM (2009) 211 final
- Recommendation on Directors' pay: C (2009) 3177
- Recommendation on Financial services sector pay: C (2009) 3159

Regulation of alternative investors

The debate on the regulation of alternative investors (especially hedge funds and private equity funds) heated up in June. At the centre of the debate is a proposal for a Directive on alternative investors, submitted by DG Internal Market at the end of April 2009. This proposal was prepared due to pressure from the European Parliament and as part of the G-20 agreement to broaden financial regulation. Although the proposed Directive has been attacked by the hedge fund and private equity associations as being too strict, others have criticised the proposal for not going far enough in improving transparency and controlling the behaviour of alternative investors.

In particular, Poul Nyrup Rasmussen, President of the Party of European Socialists, former member of the European Parliament and co-author of the 2007 study *Hedge Funds and Private Equity – A Critical Analysis*, has emerged as a vocal critic of the proposed Directive. At different events (for example, a recent conference at the Centre for European Policy Studies) he has made the following ten criticisms of the draft proposal:

1. scope: only EU managers are included in the regulation
2. the formality of the regulation: no substantive requirements
3. thresholds (100 million /500 million): exemptions not justified
4. no capital or liquidity requirements
5. insufficient transparency: no regulations on reporting
6. no real disclosure of investment portfolios
7. no initiative on market distortion by non-EU funds
8. no reporting requirements on naked short-selling
9. no specific protections for institutional investors: these investors should be not permitted to invest in funds which do not fall under the scope of this Directive
10. no provisions on tax evasion

In short, the draft Directive falls far short of requiring what would be necessary to ensure stable and sustainable financial markets in Europe.

Links:

- DG Internal Market website for Alternative Investor Regulation
- PES report *Hedge Funds and Private Equity: A Critical Analysis*
- Alternative proposal from the Foundation for European Progressive Studies

European Corporate Governance Forum

At its last meeting, in May, the Forum discussed the following topics: executive remuneration; corporate governance of banks; empty voting and transparency of investors' positions; cross-border voting and protection of minority shareholder rights – state of play. Moreover, the Forum published two statements, one on executive remuneration and one on cross-border issues arising from corporate governance codes. A challenge for future meetings will be to try to bring to the fore a perspective on worker participation as an element of long-term, sustainable corporate governance.

Links:

- Commission page on the Forum
- Statement from the European Corporate Governance Forum on executive remuneration
- Statement from the European Corporate Governance Forum on Cross-border issues of Corporate Governance Codes

Advisory Group on Corporate Governance and Company Law

The latest meeting of the Advisory Group took place on 28 April. The group discussed the EU response to the financial crisis, focusing on corporate governance and company law aspects. In this context, the Commission Recommendations on directors' remuneration have been subject to criticism. Several members of the group asked for clarifications.

The medium- and long-term actions in the field of corporate governance and company law were also discussed. It was agreed that there is no more need to reform the capital regime, having simplified the second Company Law Directive. However, the political debate on whether to completely overhaul the recent system could revive consideration of the minimal capital provisions in the SPE Regulation. In the context of corporate social responsibility (CSR) the Commission pointed out that stakeholders were increasingly lobbying for the inclusion of CSR policy measures. As examples, the Commission highlighted the push to make the disclosure of environmental, social and governance data mandatory for listed companies. Interestingly, the Commission did not mention advanced measures to safeguard stakeholder interests, such as board-level participation regimes. This is an issue which, in the wake of the recent financial crisis, should have a more prominent place on the Commission's agenda. Some members underlined the need to adopt the 14th Company Law Directive, which is also demanded by the European Parliament. The Commission pointed out that a proposal could not be expected in the immediate future.

Hopefully, the next Internal Market Commissioner will put more emphasis on this question, which has enormous importance for stakeholders. The last possible measure discussed by the Group was the choice of board structure, a topic which has been part of the Commission consultation on future priorities in the field of company law. The members had different views on this issue.

Links:

- Commission page on the Advisory Group
- Minutes of the meeting

Study on 'comply or explain'

In December 2008, DG Internal Market and Services commissioned a study on the monitoring and enforcement systems for Member States' corporate governance codes. The objectives of the study are: to describe the relationship, in the 27 Member States, between legislation and 'soft' law (codes) in corporate governance; to examine the existing monitoring and enforcement mechanisms in the Member States as far as corporate governance codes are concerned and to evaluate their effectiveness; to obtain an impression of companies' perception of the codes; and to evaluate the perception of shareholders with regard to the quality of companies' disclosure on the application of corporate governance principles and of explanations given where the company declares non-compliance, and of their reactions to disclosure which is perceived as insufficient.

The contract went to the RiskMetrics Group, in collaboration with BusinessEurope (the Confederation of European Business), ecoDa (the European Confederation of Directors' Associations) and law firm Landwell & Associés and its European legal correspondents. According to the Commission, the contractors had difficulties in obtaining replies from investors. It is assumed that the low level of feedback has to do with a lack of interest on the part of investors in these questions. The significance of this study could therefore be questioned from the beginning.

The final study is due at the end of 2009. It is planned to present it at the forthcoming Corporate Governance Conference, which will be held under the Swedish Presidency (on 2–3 December). It will be quite interesting to see if the final report will support 'comply or explain' as an adequate regulatory mechanism, or whether a more critical approach demanding binding regulation in corporate governance will predominate.

Link:

- RiskMetrics Group

Review of the SE statute

Recently, the Commission contracted Ernst & Young to carry out a study of the operation and impacts of the Statute for a European Company. The study is intended to assess the effectiveness of the SE statute from the employers' perspective. So far, it seems that there has been no effort to take employee stakeholder perspectives into account. The study should be available by the end of 2009 and be followed up by a stakeholder conference in early 2010.

However, BusinessEurope organised a roundtable on the European Company Statute on 30 June 2009, which was clearly linked to this context. Philippe de Buck, Director General of BusinessEurope, explained in his introductory speech that the exchange of experiences with representatives of companies already applying the SE regulation from different origins would lead to the consideration in the upcoming Commission report on the implementation and effectiveness of the SE Regulation. He identified one shortcoming – among others – as the 'complex worker participation arrangements'. European Trade Union experts were not given access to this event, although it was supported by the EU Commission.

Link

- BusinessEurope

Directive on cross-border mergers

The Commission has published an overview of several matters related to the Cross-Border Merger Directive. The overview contains the following issues:

- the types of company which are subject to the rules of the Cross-Border Merger Directive in the different Member States and EEA countries;
- the national authorities competent to issue a pre-merger certificate (Article 10), to scrutinise the legality of a merger (Article 11) and to register a merger (Article 13).

Link:

- Overview
- Information regarding the Cross-Border Merger Directive

National backgrounds

In accordance with the Commission Recommendations on remuneration policies, on 18 June 2009, the German Bundestag adopted a law on the appropriateness of director remuneration (Gesetz zur Angemessenheit der Vorstandsvergütung – VorstAG). The law should ensure that, in future, the sustainable development of a company is the key issue in the determination of executive remuneration and should also safeguard the long-term interests of employees, which have often been jeopardised by perverse remuneration schemes in the past. One of the key readjustments in the new law is the obligation of the whole supervisory board, and not only of a committee, to decide on directors' remuneration. Furthermore, former

managers are not allowed to become members of the supervisory board for two years. Finally, it will be easier to reclaim remuneration if a company's situation worsens.

Link:

- Webpage of the German Ministry of Justice regarding the VorstAG

Moreover, the Preamble of the German Corporate Governance Code was modified. In future, company directors shall be obliged to run the company in the interests of all stakeholders – especially the employees – and not only in the interests of shareholders.

- Further Information on the Pages of the German Trade Union Confederation

On 29 May 2009, the Danish Parliament adopted a new law which opens the boards of Danish companies to foreign employee-representatives. Similar regulations can be found in Norway and Sweden.

Number of European Companies (SE)

The ETUI has published its latest update of data outlining the number of European Companies established across the EU. After a period of incubation, more dynamic development can now be observed, with the total number of SEs registered increasing from 350 (March 2009) to 382.

Link:

- ETUI SE Factsheets Website

Books and articles

Les administrateurs salariés et la gouvernance d'entreprise

Worker directors in France – Staff representatives, shop stewards, works councillors… If actors and observers of the social dialogue sphere are familiar with information and consultation rights for workers, participation of the latter in company's administration is much less known, especially when it has to do with workers representation on companies' board as effective member, i.e. with a deliberative voice. Who are those workers directors? What are their duties? How do they reconcile workers defence with company's economic goals? What policy do trade unions, which support them, have adopted regarding this kind of "soft" codetermination? [available only in **French**] more