In this Eurosif EU Insider, we continue to examine the changing face of Corporate Governance at the EU level. Eurosif believes understanding and influencing a more equitable Corporate Governance system across Europe will better enable SEE issues to be integrated into the EU financial services sector. Much of this revolves around improved transparency.

In this issue, we highlight four areas of importance:
1. Second Consultation on Shareholders’ Rights,
2. Current Corporate Governance Agenda as presented by Commissioner McCreevy,
3. Amendment concerning the Directive on Annual Accounts,
4. EC proposals on the investment fund market.

We summarise each area by informing you of Eurosif Next Steps as a means to follow up with these important developments at the EU level.

Results of the Second Consultation on Shareholders’ Rights

This summer, DG Internal Market performed the Second Consultation on Shareholders’ Rights - following up on its previous work in the area. A summary of answers to the consultation has now been published, giving indications as to where future legislative steps might be taken.

The key results were:
- Respondents mostly favour a directive (as opposed to a recommendation) as a guarantee for implementation by member states and by companies.
- In general, DG Internal Market agrees on the scope of proposals and the level of proposed minimum standards. There are a few differences of opinion, which could narrow the scope of the legislative approach.

The Consultation revealed strong support for:
- Ownership of right to vote with ultimate investor,
- Support for minimum AGM notice periods (4 weeks),
- Generalisation of record date systems,
- Specification of content of AGM information & timely delivery of GM notice,
- Enabling voting in absentia (including electronic voting),
- Importance of post AGM communications.

The following disagreements or concerns appeared:
- Difficulty of determining who is the ultimate investor because share ownership is very diverse in the EU (However, long-term efforts towards a common definition of “ultimate investor” was encouraged).
- The translation of AGM documents, which could create unreasonable costs.
- A need to distinguish electronic participation in AGMs from electronic voting. The latter is very much supported, the former less so.
- The “democratisation” towards the right to ask questions in writing or during the AGM raises concerns as to the manageability of AGMs.

In general, respondents have again highlighted the crucial role of shareholders in holding Board of directors and management accountable. They see this as a key step to strengthening internal controls.

DG Internal Market tells us it will make decisions on future steps in the coming weeks.

Eurosif Next Steps

At this point Eurosif is waiting for the final legislative proposals from the DG Internal Market. While further action is unlikely, due to the rather consensual and technical approach developed in this process, we could consider proposing or supporting amendments that would, in our eyes, be key to strengthening cross border shareholder democracy.

Note that in the name of transparency many individual answers to the consultation, including Eurosif’s, have agreed to be published and have been made available at:
http://forum.europa.eu.int/Public/ir/mkt/irkt_consultations/library?l=/company_law/shareholders_rights&vm=detailed&sb=Title
EU Commissioner McCreevy presents outline of CG agenda

At the Second European Corporate Governance Conference on June 28th, 2005, EU-commissioner McCreevy presented an analysis of the accomplishments of the first stage of the ‘Action Plan on Company Law and Corporate Governance’, which was first laid out in May 2003.

The European Commission’s programme was based on two key objectives: (1) bringing more transparency to the way companies operate; and (2) empowering shareholders. In implementing these objectives the European Commission has endeavoured to strike a careful balance between empowering shareholders while leaving enough flexibility for management to lead companies and to get on with day-to-day business.

The medium term measures that were announced in the action plan on “Modernising Company Law and Enhancing Corporate Governance in the European Union” are:

- Enhanced disclosure by institutional investors of their investment and voting policies,
- Choice for all listed companies between the two types (monistic/dualistic) of board structures,
- Enhancing the responsibilities of board members (special investigation right, wrongful trading rule, director’s disqualification)
- Examination of the consequences of an approach aiming at achieving a full shareholder democracy (‘one share, one vote’), at least for listed companies,
- Review of the feasibility of an alternative to the capital maintenance regime,
- Framework rule for groups, allowing the adoption at subsidiary level of a co-ordinated group policy,
- Prohibition of stock exchange listing for abusive pyramids, if appropriate, following further examination and expert input,
- Simplification of the Third Directive (legal mergers) and Sixth Directive (legal divisions),
- Possible proposal for a Statute for a European Private Company (depending on the outcome of the feasibility study),
- Assess the need for the creation of other EU legal forms (e.g. European Foundation),
- Introduce basic disclosure rules for all legal entities with limited liability, subject to further examination.

In the run-up to the announcement of the European Commission’s publication of a medium term work programme it has become clear that the Commission will seek to eliminate discriminatory treatment of shareholders by introducing the principle of ‘one share, one vote’ principle across the EU. A move towards ‘one share, one vote’ would be politically explosive and will be fiercely resisted by some member states and companies. The European Commission is expected to issue a recommendation instead of proposing binding legislation. This approach is probably the only one that holds some seeds for success as one recalls last year’s defeat of the European Commission on the abolishment of multiple voting rights during take-overs (take-over directive).

Eurosif Next Steps

Eurosif is particularly concerned with matters of disclosure by institutional investors as well as by the examination of full shareholder democracy. Beyond their intrinsic value in corporate governance, they are also particularly relevant topics for SRI investors. Thus, we plan to continue our dialogue with the relevant DG Internal Market authorities. In doing so, we will be involved in the discussions and consultations, and we will ensure that the membership’s view is properly communicated.
Draft Directive on the “Amendment concerning the directive on annual accounts of certain types of companies and consolidated accounts”

The purpose of the proposal is to further enhance confidence in the financial statements and annual reports published by European companies. In this respect, shareholders and other stakeholders need reliable, complete and easily accessible information. As recent corporate scandals have underlined that urgent action is necessary, the Commission has proposed amendments to its existing legislation. It will aim, among other things, to introduce the following corporate governance statement: The Commission considers that the Corporate Governance Statement should become a specific part of the company’s annual report and that it should also indicate certain information to be given in accordance with the Take Over Bids Directive as well as information about the risk management system, the operation of the shareholder meeting, the shareholders’ rights and the operation of the board and its committees.

The “Legal Affairs Committee” (JURI) and the “Economic and Monetary Affairs Committee” (ECON) of the European Parliament are dealing with the proposal. The ECON acts as an advisory committee. This means that JURI takes the ECON report, and its amendments, into consideration for the final vote.

An ECON rapport and vote in July has supported and even reinforced Eurosif’s position to maintain the corporate governance statement as part of the annual report. Indeed, following Eurosif demands, the statement is now required to be a specific section, rather than a separate part of the report.

However, JURI rapporteur Klaus Heiner Lehne (EPP-ED, Germany) defends that costly and inefficient over-regulation should be avoided. Measures to enhance business transparency and liability for inappropriate behaviour should be proportionate to their actual benefit to shareholders and other interested parties. As a result, he has introduced amendments asking that the corporate governance statement should not form part of the annual report, but that it should be made permanently accessible as a separate legal instrument. He further considers that it should not form part of the financial statement, since this would require a management assessment. He thinks a number of the items required in the corporate governance statement to be superfluous and disproportionate, since the benefit of inclusion in the corporate governance statement would be far exceeded by the effort and costs involved.

Eurosif Next Steps

Eurosif members may be aware of previous Eurosif work with regards to these amendments. In particular, we supported the introduction of SEE wording into the Corporate Governance Statement:

"Furthermore, where relevant, companies may also provide an analysis of environment and social aspects necessary for an understanding of the company’s development, performance and position”.

In the current context, Eurosif has contacted leading MEPs in both committees insisting that the corporate governance statement should be an integral element of the annual report. Eurosif believes that the statement is an extremely important means of improving communication between companies and investors. It is more than likely to improve the overall understanding and assessment of these issues by both parties. Indeed, a growing number of long-term investors, among them, pension funds and other institutional investors, are looking at these risks and opportunities as key long-term value drivers for the companies in which they invest.

The JURI committee has continually postponed its vote on both the Lehne report and that of the ECON committee. We are now aiming for a vote in the November 2005 session. Eurosif will closely monitor the outcome of this vote, to try to ensure JURI does not succeed in removing the Corporate Governance Statement, which is essential to Eurosif. If this situation should arise, we would try and intervene with more MPs prior to the final vote in a plenary session.

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2 Accounting directives (Directives 78/660/EEC and 83/349/EEC).
3 The amendments also aim to establish collective responsibility of board members, at least towards the company and enhance transparency about related parties-transactions (as set out in the IAS 24) and enhance transparency about off-balance arrangements: In order to ensure that the true-and-fair-view principle is more clearly implemented at a European level, the Commission proposes that all companies -whether listed or not - be required to disclose any off balance sheet arrangements and their financial impact if it can be material for an investor’s assessment of a company’s financial position.
Financial services: Commission proposes improvements to the European market for investment funds

On 14 July 2005 the European Commission published a Green Paper on the enhancement of the EU framework for investment funds. The paper invites stakeholders to react to a range of proposals aimed at boosting the efficiency of the single market for investment funds. An efficient European investment fund market - where some €5 trillion of funds are currently under management - is of key importance in the context of enhancing investment and in contributing to better provisioning for old age.

The Green Paper reviews the functioning of the legislative framework for investment funds provided for by the UCITS Directive (Undertakings for Collective Investment in Transferable Securities), which seeks to enable a fund authorised in one Member State to be sold across the EU while assuring a high level of investor protection. The Green Paper analysis, based on extensive research, draws on wide-ranging consultation with market participants and national authorities.

The European Commission emphasises that the European investment fund market is of key importance to the citizens of Europe, also affecting their future welfare. In some Member States 20% of the adult population invest in funds. The EU framework for investment funds has made a significant contribution to the success of this market. Today, some 28,000 UCITS amounting to some € 4 trillion represent more than 70% of the assets under management by the European fund industry. Despite these achievements, there is scope for improvement.

However, a central message of this Green Paper is that there is no compelling case at this stage for fundamental legislative overhaul. Instead the paper identifies concrete short-term measures to ensure consistent implementation and more efficient operation of existing rules.

In the longer term, the EU fund industry is facing unprecedented structural challenges. There is also promise of new opportunities. The growth of other types of collective investments and the need for a cost-effective organisation of the EU industry may call for new answers. The Green Paper seeks to stimulate debate on whether an EU-level response is required and, if so, whether to legislate or issue recommendations.

The Commission invites comments on this Green Paper. Contributions should be sent by 15 November 2005 to: markt-consult-investmentfunds@cec.eu.int

In addition, an open hearing was held in Brussels on 13 October 2005. Following analysis of the contributions, the Commission will publish a definitive statement of future action. At the event, EU commissioner McCreevy announced that the European Commission planned to set up the two expert groups: one on alternative investments and one on the rationalisation of the investment fund value-chain. The European Commission will shortly be asking all interested associations able to mobilise expertise in these fields to nominate possible participants.

Eurosif Next Steps

As it stands today, the proposal does not contain a reference to SRI. Eurosif will however continue to monitor this effort as it may have impacts on our members’ activities. In addition, where appropriate we will ensure that authorities are aware of the Eurosif Transparency Guidelines. These could, if needed, play a role in ensuring the investor protection demanded by the Commission with regards to SRI products.

Eurosif will contact the European Commission for more information about the planned expert groups and in particular the one on “alternative investments”.