



a.s.b.l.

Confédération Européenne des Associations d'Administrateurs
European Confederation of Directors' Associations

ecoDa response to the EU consultation on Company Law

POINTS OF ATTENTION PUBLIC CONSULTATION EUROPEAN COMPANY LAW, 1st June 2012

1. Private, public and listed companies

- From a purely legal perspective, a distinction between a private and a public company might be relevant as far as the legal form of a 'company' is concerned.
- But for the purpose of Governance Recommendations and laws, the distinction between a listed and an unlisted company is far more relevant than the private/public distinction.
- Governance challenges and recommendations differ considerably between listed and unlisted companies. However, there should be more attention given to the following issues:
 - Listed companies are not a homogeneous group. They do not face the same governance challenges in all EU countries (and challenges may differ even within Member States). One of the main differential factors is the degree of shareholding concentration as well as the typology of the main shareholding blocks. A more nuanced approach is necessary in relation to the relevant governance mechanisms (e.g. greater focus on issues relating to shareholder activism and short term thinking in a model with highly volatile and dispersed shareholding versus the need to take account of private benefits and related parties transactions in models with controlling shareholders).
 - Proportionality should be built into the system, in relation to the size of listed companies and the risks involved (cfr. systemic banking institutions). However, economic importance might also be an important discriminating factor. Recommendations might need to become mandatory for unlisted companies if they are considered sensitive and economically important business firms (cfr. subsidiary companies in sensitive sectors like financial sectors, utilities).
 - Attention should be given to potential distortion of the level playing field between competing firms. This might arise due to the fact that listing on a

ecoDa

a.s.b.l.

Confédération Européenne des Associations d'Administrateurs
European Confederation of Directors' Associations

regulated market becomes overly burdensome in comparison to listing on an alternative market or remaining unlisted. Moreover, politicians seem to adhere to the misconception that listed companies are part of the 'public domain'; ignoring the fact that (most of the time) they are private property. To take stock of potential distortions, critical cost-benefit analysis on a periodic basis is essential.

- The diversity of corporate governance models reflects the complexity of modern business enterprises. This diversity should not be viewed as an obstacle, but as a treasure, proving that different solutions exist to a wide variety of business challenges.
- On the basis of the same line of thinking, we should not seek a complete European harmonization of governance regulation and corporate law, but rather favor flexibility by stimulating Member States to consider policy options from other jurisdictions to supplement their national solutions.

2. **The need for investors to make an increased contribution to governance and the long term viability of companies** may require that amendments are made to the by-laws or the governance charter of (some) listed companies:

- This challenge is quite different in listed companies with more volatile shareholders (institutional investors, share traders, hedge funds ,....) compared to firms with controlling family shareholders (with a much longer term focus).
 - While not ignoring the importance of institutional investors to the funding and operation of stock markets, efforts should be made to foster long-term ownership.
 - Companies should be allowed to provide for a preferential treatment of long term shareholders, by means of enhanced voting rights or higher dividends (within certain limits, see e.g. France).
 - Additionally, coordination efforts between companies and their (long term) shareholders should be promoted. This could require a review of existing rules on sharing inside information and acting in concert..
- Whatever the shareholding structure, it is the duty of the board to devote sufficient time to developing a long term viability policy, while also taking the short term imperatives of the business and its shareholders into account. The annual governance statement should give a clear description of such policy and its execution in practice.

ecoDa

a.s.b.l.

Confédération Européenne des Associations d'Administrateurs
European Confederation of Directors' Associations

- The structure of variable executive remuneration is an important driver to influence the short versus long-term thinking and the risk aversion (or excessive risk-taking) of top management.
- While quarterly reporting may create transparency to the market, more emphasis could be placed on encouraging the disclosure of non-financial information that highlights the long-term viability of the company.
- More attention should be paid to the unintended consequences of accounting standards, such as the potential negative effect of the distribution of unearned income (to shareholders in the form of dividends and share buy backs, and to management in the form of variable remuneration-).
- Long term viability requires that the board pays more attention to appropriate levels of provisioning and leverage. Options should be tested under different stress scenarios.

3. Corporate governance and the position of independent directors

- It is a matter of good governance and effective ‘checks and balances’ that shareholders have the right to nominate and dismiss directors. The dismissal of directors at will (at nutum) is a legal principle in different European countries (e.g. Belgium, France). If such a system of ‘dismissal at will’ exists, ecoDa wants to stress the need for integrating into the respective corporate governance codes some safeguards to guarantee that such rules do not hamper the independent attitude of directors, e.g. by providing enough transparency in case of any premature dismissal of independent directors.
- However, it is also clear that the role and functioning of independent directors has been under attack, not in the least in the slipstream of the financial crisis. A more critical evaluation of the independent behavior of directors might be far more important than any stringent a-priori check of the formal independence in comparison to a detailed list of independence criteria. Such list of independence criteria might need more in-depth research, because it has mostly been the product of a copy-paste approach, far more than any thorough reflection on what drives independence. Moreover, independence is only one essential component of the diversity and competence needed to stimulate good governance. Business knowledge and sectoral expertise should never be substituted by a purely independence focus, while a board mandate might need quite more professional development and training than assumed

ecoDa

a.s.b.l.

Confédération Européenne des Associations d'Administrateurs
European Confederation of Directors' Associations

so far. Therefore the European Commission might investigate the need to promote the creation of a 'certified' director.

4. One versus two-tier boards

- As highlighted before, the European Commission could stimulate its Member States to enlarge the portfolio of governance choices to allow legal formats and organs that exist throughout the EU. One specific point of attention in this respect is the liberty to organize one's governance along the structure of a one-tier or a two-tier board. Such flexibility should be allowed for listed as well as for unlisted companies.
- Whether firms opt for a one-tier board or a two-tier board, there should always be a clear delineation between the responsibilities of (non-executive) directors and managers (executive board). To this end a division of responsibilities for chairing the one-tier board from the chair of executive management is an additional element, if opting for a one-tier board. Here smaller unlisted companies might (want to) deviate from this, but nevertheless they should be stimulated to clearly distinguish the duties of the board from those of management, including the leadership role of those two business functions.

5. Governance in groups of companies

- The governance recommendations focus on the single company structure (with the board in between of management and shareholders), but reality is that –certainly for listed companies- such single structures do not always exist, because groups of companies are the prevailing form for the organization of business activities throughout Europe. Therefore the European Commission should pay more attention to the 'internal' governance within groups of companies.
- A special point of attention is the position of the 'external' director in the board of a subsidiary company (listed or unlisted). While such director should focus on the interest of the subsidiary company, group management and group interests might force him to accept sub-optimal choices, decisions or transactions. Here more strict guidance on how to reconcile the interest of the subsidiary company with the group's interest and the corporate interest of the Headquarters is more than necessary.
- A clear indication should be given in the annual governance statement of the (listed) mother company of the model used to govern and manage the group. This governance statement should provide full transparency of the group structure and the type of shareholding in subsidiaries and joint ventures (direct as well as indirect control

4

ecoDa

a.s.b.l.

Confédération Européenne des Associations d'Administrateurs
European Confederation of Directors' Associations

should be indicated), including also information on the respective board structures and composition (indicating whether directors are internal (management responsibility within the group) or external/ independent). Special attention should be paid to intra-group relations and related-parties transactions.

Lutgart Van den Berghe, President of the Policy Committee
Béatrice Richez-Baum, Secretary General

ecoDa, the European Confederation of Directors' Associations
rue de la loi, 42
1040 Brussels (Belgium)
contact@ecoda.org
Tel: 02 231 58 11
Fax: 02 231 58 31