Corporate governance framework for European companies

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The Committee on Legal Affairs adopted the own-initiative drafted by Sebastian Valentin BODU (EPP, RO) on a corporate governance framework for European companies, in response to the Commission Green Paper on the same issue.

Welcoming the Commission's revision of the EU corporate governance framework initiated by the Green Paper, Members regret, however, that important corporate governance issues such as board decision-making, directors' responsibility, directors' independence, conflicts of interest or stakeholders' involvement have been left out of the Green Paper. They also regret the Green Paper's focus on the unitary system and disregard for the dual system, which is equally widely represented in Europe.

Members underline the importance of the following issues:

- creating a more **transparent, stable, reliable and accountable corporate sector** in the EU, with improved corporate governance;
- the need for **independent auditing and rules** respecting the different corporate cultures in the EU;
- the importance of creating a more transparent, stable, reliable and accountable corporate sector in the EU, with improved corporate governance;
- that it is a prerequisite that a well-governed company should be accountable and transparent to its employees, shareholders and, where appropriate, to other stakeholders;
- that the **2004 OECD definition of corporate governance**, according to which corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders, should be further promoted;
- that a **basic set of EU corporate governance measures** should apply to all listed companies; these measures should be proportional to the size, complexity and type of the company;
- that initiatives on corporate governance should go hand in hand with the initiatives on **corporate social responsibility** proposed by the Commission.

The Commission is called upon to submit every legislative proposal it considers on corporate governance to **impact assessment**, which should focus both on objectives to be attained and on the need to keep companies competitive.

(1) Boards of directors: the report stresses that in unitary systems there should be a **clear demarcation between the duties of the Chair of the Board of Directors and the Chief Executive Officer**; however, it notes that this rule should be proportional to the size and the peculiarities of the company.

The boards must include **independent individuals** with a mix of skills, experiences and backgrounds, that this aspect of their composition should be adapted to the complexity of the activities of the company and that it is the responsibility of the shareholders to ensure the right balance of skills in the board.

The report considers that directors' pay rises should be consistent with the long-term viability of their companies. It supports the inclusion in managers' variable remuneration of long-term sustainability components, such as making a percentage of their variable remuneration dependent on the achievement of corporate social responsibility targets, e.g. health and safety in the workplace and employee job satisfaction.

Members believe that strong surveillance and new rules must be introduced to **forbid any malpractices concerning the salaries, bonuses and compensation paid to executives** of companies belonging to the financial or non-financial corporate sector that have been bailed-out by a Member State government.

(2) Shareholders: Members believe that shareholders' engagement with the company should be encouraged by **enhancing their role**, but that this involvement should be a **discretionary choice** and never an obligation. Nevertheless, they believe that measures to incentivise long term investment should be considered and also a requirement for full transparency of voting for any borrowed shares, apart from bearer shares. They consider that institutional investor behaviour aimed at creating liquidity and keeping good ratings should be reconsidered, as this solely encourages short-term shareholding by such investors.

The report notes that there is a lack of long-term focus within the market and urges the Commission to review all relevant legislation to assess whether any requirements have inadvertently added to short-termism.

The Commission is called upon to:

- bring forward proportionate proposals for **Europe-wide guidelines on the type of information released** to shareholders in annual company reports; in this context, the report notes that **conflicts of interest**, including those of a potential nature, should always be disclosed and that appropriate action is needed at EU level;
- **amend the Shareholders' Rights Directive** in such a way as to evaluate by what means shareholders' participation can be further enhanced; considers, in this connection, that the role of electronic voting at general meetings of listed companies in order to encourage shareholders' participation, especially with regard to cross-border shareholders, should be analysed by the Commission through an impact assessment;
- ensure further regulation of **proxy advisors**, giving special attention to transparency and conflict-of-interest issues.

Members consider that companies should be **entitled to choose between a name shares regime and a bearer shares regime.** They consider that, if they choose name shares, companies should be entitled to know the identity of their owners and that minimum harmonisation requirements should be set at EU level for the disclosure of material shareholdings.

Lastly, Members consider that the question of employee share ownership schemes is one which should be regulated at Member State level and left to negotiations between employers and employees: the possibility of participating in such a scheme should always be of a voluntary nature.

(3) The 'comply or explain' framework: Members believe that this system is a **useful tool** in corporate governance. They are in favour of compulsory adherence to a national corporate governance code or a Code of Conduct chosen by the company; considers that any deviation from the Code of Conduct should be explained in a meaningful way and that, in addition to this explanation, the alternative corporate governance measure taken should be described and explained.

Lastly, the report stresses the need to achieve **better functioning** of, and compliance with, **existing governance rules and recommendations** rather than imposing binding European corporate governance rules.