European Corporate Governance Conference, 14th November 2005 Mermaid Conference Centre, London

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PROGRAMME

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Questions and Comments from the Floor (please note, Jaap Winter and Gerhard Cromme had to leave before the final plenary discussion).

Summing Up: Pierre Delsaux, European Commission

in association with HERMES

Keynote Speech by Commissioner McCreevy

I am delighted that the UK Presidency has chosen the future priorities of the EU Company Law and Corporate Governance Action Plan as the subject for today's conference. I am also impressed that the Presidency has managed to gather so many experts on a Monday morning to discuss what some might regard as a rather dry subject. In fact, I'm sure that the nature of your debates today will show that it is anything but dry….

We are approaching the end of the first phase of the Action Plan. The timing is perfect to start a reflection on what should be done in the second phase. That is why the Commission will launch, in the next few weeks, a wide-ranging public consultation. This Conference is the first step in that consultation. We already want to hear your views today. I want to be able to benefit from the considerable expertise and collective wisdom of all those present. And I hope that you will take the time to follow up with detailed comments and suggestions in response to our consultation document. Once the consultation document is issued, there will be a three month period for comments. My door (and particularly that of my staff!) will be open even wider than usual during this period.

Before I address future priorities, I should start by saying something about the first phase of the Action Plan. How well have we done in keeping to the priorities set?

I think it is fair to say that over the past two years, the short term priorities in the Action Plan have been successfully implemented. Priorities and timing have been respected. We are putting the finishing touches to a couple of the outstanding measures. For example, the modification of the accounting directives which I hope will be adopted by the end of the year. This will, amongst other things, allow stakeholders to get a clearer picture of a company's corporate governance practices by requiring companies to disclose whether they follow a corporate governance code and where they depart from it. We are also finalising our initiative to facilitate the cross-border exercise of shareholders' rights. Our objective is to try and get the plumbing right so cross-border voting can flow across borders. I intend to submit a draft directive to my colleagues in the Commission by the end of the year.

The main underlying principles in the Action Plan have been twofold: (1) enhancing transparency; and (2) empowering shareholders. These principles will remain equally valid for the second phase. I am convinced that their application will help companies to attract investors and, as a consequence, enable them to increase their production and incidentally their profitability.

However, the short term priority measures were fixed when we were in the business of enhancing investors' confidence after the financial scandals at the beginning of the millennium. The priorities very much reflected this: improving the framework for EU audit, confirming the responsibility of the board for financial and key non-financial statements, more transparency on directors' remuneration, strengthening the independence of directors etc.

The context in which we will set our priorities for the second phase is very different. Restoring investor confidence is no longer the main driver. The impetus for what we do next at EU level must now be the tandem of: (1) improving the competitiveness of EU companies- the so-called Lisbon agenda; and (2) the EU's push towards better regulation.

A few words on the competitiveness angle. Despite having an Internal Market of over 450 million, we still make it difficult for companies to exploit this. We need more entrepreneurs and we need to make it easier to set up, and to wind up, businesses. Let's face the facts. How easy is it to do business in the EU? Comparatively, not very. According to the World Bank, only two Member States figure in the world's top ten countries and eleven in the top thirty. This simply is not good enough: it is not going to get the EU as whole to the top of the league. Much of what needs to be done lies in the hands of the EU Member States. But the EU must not shoot companies and Member States in the foot as they try to get out of the starting block.

If we have a competitive internal market, our firms will have better chances of competing successfully abroad. Globalisation might then be perceived not as a threat but as an opportunity. The priorities we now set in the Action Plan must be conducive to entrepreneurship and making the most of the potential of the international dimension.

Better Regulation is a very important part of trying to get the climate right for business. Talking about Better Regulation in London is a bit like "taking coals to Newcastle", or perhaps even "teaching your Grandmother to suck eggs". You have, of course, just hosted, at the end of September, a two days' conference on this issue. However, Alan Johnson said recently that the challenge would now be to put all these words into actions and this is what I want to focus on now: how can we walk the talk on Better Regulation in the field of the internal market policy and what does it mean for the Company Law Action Plan?

In my view, it means four things.

Firstly, it means consultation with stakeholders, about which I have already spoken.

Secondly, it means only legislating at EU level when that is the best level at which to act and where legislation is the only answer. We need to opt for instruments that put the least burden on companies and leave them as much flexibility as possible. Therefore, we will prefer a recommendation to a directive where a recommendation is suited to achieve the aim pursued. We will look at the measures originally proposed to see if they are still appropriate. For example, whether a directive is really needed on disclosure for institutional investors or whether the market is already moving in the right direction…

Thirdly, it means a comprehensive impact assessment for any new piece of legislation to be submitted to the Commission. This builds on what is now becoming standard practice. Thus, if the Commission adopts a proposal for a directive on shareholders' rights, it will at the same time approve a detailed impact assessment that will properly assess the benefits and costs for the parties concerned. I believe that the impact assessment is an indispensable tool for improving the quality of our work.

Fourthly, better regulation means we will be adding a new dimension to the consultation on the Action Plan. Three weeks ago the Commission adopted a three year rolling programme of measures to simplify existing EU law as one central element of our Better Regulation project. The existing Company Law Directives are part of this exercise.

Company Law must be accessible and comprehensible. Moreover, most of European Company Law was designed from the late 1960s to the early 1990s. In the meantime markets have changed. So have the needs of companies and stakeholders. Our idea is to work on the adoption of a single legislative text which modernises and simplifies the company law directives by eliminating any dead wood together with any contradictory, overlapping and outdated provisions.

I would not like to disappoint you by failing to mention, before closing, the issue of "one share, one vote". I would be delighted, by the way, if all announcements from Commissioners in Brussels would trigger the same enthusiastic reaction in the UK press as my uttering of these words a few weeks ago. For me, the shareholder is king or queen: this goes back to what I said at the beginning about transparency and shareholder empowerment. If these principles are followed, I am convinced it will lead to companies which are better run. Pricing of shares on exchanges confirms that this is what the market tends to think. But I am not naïve. I have heard about the fierce debates at the time the Takeover bids Directive was negotiated and I have met the people who bear the scars. I believe, nonetheless, that this should not prevent us from looking into the merits of this principle. We are in the process of commissioning an outside study and our experts in the European Corporate Governance Forum, about which we will hear more this afternoon, are already looking into this issue.

Ladies and Gentlemen, to conclude. I have posed a number of questions and only given a few hints on how I think they might be answered. Your job today is to help us formulate the answers. I would ask you to keep in mind the guiding principle that that our European companies need and deserve a modern and flexible company law framework. We must give it our best shot because they deserve no less.

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A Business Perspective: Anthony Burgmans, Chairman, Unilever

What better way to start a Monday morning in London than talking about corporate governance. I would also welcome Commissioner McCreevy's remarks and I'm sure his detailed conversation will enhance the probability that we'll get a good directive and also that the implementation will be better.

My first point is that corporate governance and competitiveness are very much linked: corporate governance can play a positive role in competitiveness but it can also play a negative role. A well-organised board conducted in a transparent way can bring skills and insights at the highest level of the company, which, in the end, will improve decision-making and which will improve the competitiveness of that particular company. Cumbersome, over-elaborate inflexible corporate governance will do exactly the opposite. It can promote the minimalistic view, it can promote the box-ticking mentality, and it could have a detrimental effect on competitiveness. Any legislation in this area should be subjected to a very careful benefit analysis before it is adopted.

The second point I want to make is that corporate governance is not only about risk insurance and the key message here is that we have to find the right balance between legislation on the one hand and competitiveness. Let me give you a few examples. The debate about what is better, a one tier or a two tier board can be quite emotive. But, the fact is that both systems can work very well provided that the spirit of that particular system is respected and implemented properly. I don't think we should waste time on arguing which is best: I think we should accept that within our community, the European community, various systems can play, but we must make sure that transparency and flexibility is there, and that they are properly implemented.

We must enable cross border development. At the moment that is very difficult. There is also lack of communication in the chain of security holders; I understand that the banks are not very enthusiastic about this whole topic because it would mean more work for them, but it is essential. If we want to see our European market as one market, we must make sure that we get easy European involvement for shareholders.

The next point I'd like to make is the national codes and the regulation. We have just seen a wave of new codes coming in. You have the combined codes in the UK; you have different codes in the Netherlands, in Germany, in France….. And we are now in the process of implementing them, in corporate business life. My plea is please give us time to do that properly and to learn from it, before we reach the next stage of changes. I admit, that as can be seen by some of the corporate scandals that Commissioner McCreevy has already alluded to that business doesn't always have a good reputation, and I know that business in general has a lot to answer for. But, nevertheless, I would like to make a plea here: give us an opportunity to implement what is already put in place now properly before we start with the next phase.

Another point is the whole issue about flexibility: we have to understand that no two countries are identical. They are living organisms: they change all the time; they have their roots in different cultures. So, in any legislation on this path, or any directive on this topic, I would very much encourage and embrace the principle of comply or explain. It allows companies to shape the corporate governance in the way you can shape a suit around a person's body. And if they do deviate from what is practised, you can then suggest to the shareholders in the shareholders' meeting and ask them to vote on it. And if the shareholders then agree, and if they are reassured that there are very good reasons for this, then I think there should be no reason to be worried about that. So I think it's very, very important that we continue to adopt this principle - that is, comply or explain.

And so, to close, let me say, the importance of corporate governance cannot be underplayed. It is indeed a very important topic and a fundamental basis, for transparency - and transparency is absolutely key. That chapter in Unilever's Annual Report is larger than in the first Annual Report which we published 75 years ago, so we have come a long way. And we have no problem with that; we have nothing to hide. We do nothing of which we are ashamed, so transparency for business life in general is no problem whatsoever, and corporate governance can give us that. Corporate governance is also a direction for the internal organisation. This means you can shape your internal organisation and organise the way decisions are taken at the top and how people are being held accountable. And finally, it is an important signal to the employees, in terms of integrity.

So yes, corporate governance is important, it is fundamental, but let me also say (and this may be a bit of a disappointment) even if you have the best corporate governance in the world, it will not be a guarantee that you won't see scandals in the future. Unfortunately, behaviour or integrity cannot be forced through codes or legislation. The best way to ensure integrity is to make sure that you have a healthy corporate culture set from the top, and a transparent and open company.

The Investor's Perspective: Jean-Pierre Hellebuyck, Vice Chairman, AXA Investment Managers

For an investment manager in Europe, the most obvious action in terms of corporate governance is to vote at general meetings, and I think also that it's part of the core business of the investment manager. Why? Because it's a way for the fund manager to protect his own interests and his customers' interests. It's also a way to engage, to develop a dialogue and knowledge with the companies. I think also that movable basis voting at general meetings and the action of shareholders helps to create the change, as other things such as integrity and the efficient operation of financial markets. And therefore I think it is very important to develop and to enhance and to remove barriers to the cross border side of shareholder rights.

What are the points which are important as an investment manager? The first point is the removal of shareholder blocking and the introduction of recording. The vast majority of investment managers favour the introduction of a record date. Also I think the majority think that this record data should be as close as possible to the original meeting. The reason is obvious; to avoid the shareholders that have sold already their shares going to the general meeting to vote. We favour, I think, generally, a day-minus-three record date. Why? Because it's very close, it compares to the short settlement and transfer of the property cycle.

The other aspect I would like to stress is that it is very important for investment managers and shareholders, as a rule, to have sufficient notice of a meeting so they are able to participate. And I think that no less than 21 business days or 30 calendar days, is absolutely necessary. If I take the example of my company, we have voted this year at up to 800 general meetings, and therefore we were obliged to use a voting platform, and very often when it comes to cross border meetings, the cut off date is two weeks which can make it impossible to vote.

I think also what is very important before the original meeting is to receive appropriate information and to be sent this early enough. I think it has to be in two languages: in the local language, of course, and also English. I know that for small companies it might be a deterrent to get listed, but if you don't understand the documents you receive, it is a big drawback to effective voting. I think we should have more dissemination of information on the internet to help develop cross border voting. And I think that companies should make the effort to explain their resolution, to explain clearly what is at stake, what is the economic issue in the resolutions.

I think it is interesting for shareholders to be able to add items to the agenda and submit resolutions, and I think thresholds shouldn't be too high against the expression of the shareholders. Again, the internet can play a major role. Communication is very important after the original meeting. Very often we have to wait a long time to know what has been the result of the voting.

To finish, I think generally in the investment management industry, we favour the removal of inequities such as limitation to voting rights and super majority voting. And, two ideas for the long term: I think we need to take into account in Europe that there are major differences between the shareholders' rights. For instance, in UK and in France I think that the *majority* of shareholders have a lot of rights; in some other countries, *some* of the stakeholders have a lot of rights like in the Netherlands or in Germany, and I think in the long term - we should try to have some form of organisation to have this kind of cross border holding.

To finish with, I think that in terms of investment inequities we should enhance and favour and encourage long term holding of equities. Equity investment is a long term process and I think in recent years this investment has become too short. And if we want to give full meaning to corporate governance and to the shareholders' voting, I think investment equity should be put more in the long term perspective.

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An Employees' Perspective:
Reiner Hoffman, Deputy General Secretary, ETUC

Workers and employees are an important group of stakeholders. Key objectives are to decrease corruption, to increase investors' confidence, not only investor confidence but also consumer confidence and to contribute to the ambitious objectives of the Lisbon Agenda.

I'd like to start with a quote from the Joint Social Partners Declaration we submitted to the Spring Council in March this year. As we said, together with the employers' organisation UNICE and CEEP, The Lisbon Strategy is about improving our competitiveness in high added value products and services, and, more generally, about securing Europe's place on the world markets by moving up the ladder on innovation, technology and productivity.

Europe cannot compete with low wage countries for labour-intensive products. If we share such a concept, then our concept of competitiveness is a much broader one and the European Company Law can contribute significantly in the general objectives we have agreed upon. EU Company Law initiatives should therefore endorse the emergence and evolution of a European model of corporate governance, fostering company boards' orientations towards long term value creation, high trust labour relations, participation of employees in the company decision-making process, and societal responsibility. Not only shareholders but also workers, other citizens, and the community at large have an interest in good governance of companies.

The European Corporate Governance Framework should provide proper institutional conditions for companies to foster long term profitability and employment prospects, mechanisms to prevent mismanagement and transparency and accountability with regards to investments and their returns. The globalisation of product markets and financial markets cause countries with different legal corporate governance frameworks to compete with one another to attract investment. Financial markets are driving companies to give centre-stage to maximising profits and increasing shareholders' value in the short term. We, as the ETUC, however, think that a corporate governance model that motivates capital and labour to agree on all-important elements of the company's policy; ensuring that management will perform better in the long run. It is precisely by means of such a model that polarisation within the company will be prevented, as well as polarisation from society towards the company. It introduces stability and enables orientation to long term goals. An important, basic contribution of the European Union to corporate social responsibility is to establishing and maintaining a well balanced corporate governance framework by legislation. We need a different approach to the shareholder model, an approach that aims at finding a balance between the different interests and which looks at the labour force as human partners, as human capital, and consequently as partners for business.

There are four essentials for a sound corporate governance framework from the ETUC's perspective. First, the board takes an independent position in such a way that it does not become driven by stock market forces. Second, the executives are subject to expert and independent supervision by non executive supervisors who form a buffer between management and shareholders. Third, the non executives and supervisors are appointed in a way that guarantees expertise and independence from management, and sets them at arms' length from the stakeholders. Fourth, an institutional role is given to the employees in the company's decision-making system.

Workers, as we know, are concerned with corporate decisions in different ways: as employees, as business partners, as investors, but also as citizens. When it comes to workers' participation rights, I'd like to remind you that we have, in 12 member states of the European Union, a vast dissemination of participation and rights. In another seven countries, we have limited dissemination of rights, including countries like Poland, France and Spain, and there are only nine countries, where we don't have participation rights at the company board level, unfortunately one of these is the UK, but also Belgium and Italy.

There has been a study conducted on behalf of the European Trade Union Institute, our research arm, concerning the economic performance of EU countries according to strength of board representation rights. Taking four main indicators; the balance of trade in relation to GDP, the degree of inequality, the strike rates, and the business competitiveness index of the World Economic Forum, results show that countries with strong worker participation rights are performing economically much better. Giving only two examples: in terms of strike rates in countries with strong rights, we have only ten days per 1,000 work days per year; and in countries with weak or no rights, we have one in five strike days per 1,000 work days. The second result is that the trade balance for countries with stronger participation is much higher in comparison to those countries with weak rights. I can't go into detail, and I wouldn't argue that strong worker participation rights are necessarily a precondition for good economic performance, but the study showed that at least it doesn't hinder a good economic performance.

If it comes to the EU policy in the field of corporate governance, we think it must be reassuring and needs clear direction. On the one hand, you've got the directive on European Works Councils; and we've got the compromise from the European company status including the directive on workers participation rights which emphasises that so much corporate governance needs management… labour relations… and, at the same time, we've got the 10th directive on mergers. Unfortunately, we didn't succeed in defending what we had agreed as a compromise on the European company status, and we are faced with the 13th directive on takeover bids and the 15th directive on transfer of seats. This must be coherent, this employees' participation rights, and this is one of the major methods we would like to give as the ETUC to the conference.

A Perspective from the European Parliament: Klaus-Heiner Lehne, MEP

Commissioner McCreevy, President Barroso and Vice President Verheugen have very often mentioned their intention to change their general attitude on legislation. The principle of the future is: less means more. Therefore, the Action Plan of the European Commission on company law has to be re-examined and reviewed. It is quite clear that under the new principles of Better Regulation the strategy and focus must be set on reducing the burden for European players. Thus, it is not very likely that the 21 different measures of the existing Action Plan will be finished until 2009. It is, however, quite likely that the new communication of the Commission will try to re-orientate the Action Plan and to set new priorities for legislative or non-legislative activities in the field of company law. Everything will follow the principles of subsidiarity, effectiveness, and necessity, and the reduction of bureaucratic burden.

The latest activities of the Commission in preparation of the Legislative Programme for 2006 are already moving into that direction. But I may say on this occasion that the official strategy declarations of the Commission are not always in direct connection with the existing legislative activities. When I take a look at the current discussion on the 4th and 7th directive, especially on the question of the additional burden for small and medium enterprises, I am not quite sure that all services within the Commission and even within Council take those strategy guidelines very seriously.

The Parliament is in principle supporting the new general approach of the Commission. Probably many of us in the Parliament are even more supporting this approach than the Commission itself.

Now let's come to the specific items on the Action Plan, from which I believe they should be in the focus of priority setting. I will name them point by point giving a short comment.

1. Directive on the transfer of the registered office

This directive is long overdue. Even decisions by European Court of Justice have not solved the problem. Under European Court of Justice ruling, you may have the registered office of your company in one member state, and all business operations are run in another member state. According to the Cross-Border Mergers Directive, you may merge your company into another Member State. With the European Company you may create a new legal entity anywhere in the European Union. But one thing you still cannot do: you still cannot transfer a company to another Member State. I do strongly believe we need this directive as soon as possible. The key problem of co-determination and workers rights could be solved in a similar way like we did with the cross border mergers directive.

2. European Private Company

This is strongly supported by the European Parliament. The background is clear. Right now, we have done a lot of legislation in favour of the big shareholder's companies. However, so far we have failed to do enough in favour of smaller and medium sized private enterprises. For them a legal structure for a European private company would open opportunities. This is not an additional bureaucratic burden but another opportunity, a right of choice between different structures.

3. Cross border exercise or shareholder’s rights

We are expecting a Commission proposal within the next weeks. This is a key item, because: as regards the excercise of cross border shareholder rights we are still more or less living in the middle ages. We are not using the technical opportunities we have already at hand. And in national legislation, there is still a lot of burden that harms cross border investment. Hence we need some movement in that direction; but it must fit into the national systems and should not bring additional bureaucratic burden. In the past years, we did a lot to increase transparency for cross border investment - not only for institutional investors but as well for smaller investors. The next logical step is obviously that we create the opportunity to open the door for the exercise of voting rights.

4. One share one vote / shareholder democracy

I personally believe that this is another key item for the development of an open and effective financial market within Europe. We already had this discussion when we had to legislate on the Takeover Directive. Without solving this problem, it will never be possible to open all markets for investment. The reason why the Takeover Directive is written as it is, is the lack of enforcement of the principle of “one share one vote”.

5. Choice between monistic and dualistic Board structure

From my point of view, the recommendation of the Winter Group plays another important role on the development of the European company law system. Right now we have already two opportunities for some companies in the different member states. The Cross Border Mergers Directive and the European Company have opened opportunities in that direction. National legislation does already exist, e.g. in France and Italy; here companies have the right of choice for one or the other system. We will probably have to discuss this problem again in the transfer of seat directive. Under these conditions it probably makes sense to open the opportunities for all European companies. I also believe that the Winter Group listed this proposal for good reasons.

6. Transparency of institutional investors
Another key item of the action plan should be transparency rules for institutional investors. General aspects of the investment policy as well as voting policy should be transparent. Another aspect which demands transparency is the question of ownership of shares. I do not think it is beneficial that the boards of big companies do not know anymore who the actual owner of the company is. More or less secret operations by hedge funds or other institutional investors show that there is a necessity for more transparency. We must provide the leadership of companies with the opportunity for a good investor relationship. The discussion last year about the control of hedge funds within Germany showed that there is a necessity move into this direction. National legislation will not help very much on that point, because the most critical activities are cross border activities, so that we need European legislation on that matter.

7. Directors responsibility and liability

The ruling of the European Court of Justice makes it necessary, that we have common rules on the question of director's disqualification. It must not be possible that a disqualified director just goes cross border and starts the same bad business again. I have my doubts, whether we are really in need of European rules on wrongful trading or other strong liability rules. This could be left to national legislation, which partially covers those problems through insolvency.

8. Directive on groups and group's policy

I personally believe the Commission should study the subject further, because most operations of big companies are already group operations. If they believe, that there is additional action required, they should do so. On pyramid structures, where the Winter Group supported legislative action by the Commission, I personally have doubts whether or not legislation is necessary. This is more or less a specific national problem in some member states. As long as we have not solved the one share one vote principle, I do not see any absolute necessity to forbid such structures by European legislation. It is even difficult, because in certain branches pyramid structures are supported or sometimes even required by national law e.g. in the insurance market.

9. Other legal private entities

The mutual company should not be part of the 68-list of the European Commission. This has nothing to do with the reduction of bureaucratic burden. It is just offering another legal opportunity for companies which want to use this choice. I agree that this is a question of personal resources within the Commission and within the member states. But that does not mean that we should quit this idea for good. This item, however, could have a lower priority and legislative work could be done later, when the more important issues are finalised.

10. Recommendation on independent directors and on the Remuneration of directors

The Commission acted on both aspects with recommendations; and normally a recommendation is just a threat in the direction of possible legislation. To make it clear, from the point of view of a European parliamentarian, the recommendation on independent directors has the quality of a dream world. Such a person as required in the recommendation does not exist and does not fit into the reality of corporate governance. E.g. in the supervisory boards in Germany, there are members on the capital side, who have the job to control in the interest of the owners and who are normally closely connected to the owners. To require someone here who is independent - and independent is more or less defined in the recommendation as knowing nothing and never having contact with the company - is unrealistic. It is quite clear, that owners control companies through the boards, especially in dualistic structures through the supervisory board. To make it clear, if the Commission is going to start a legislative proposal in line with this recommendation, there are from my point of view zero chances that such a directive will pass legislative chambers. I have much lesser problems with the other recommendation regarding the remuneration of directors. This item is actually more or less already being discussed in public and even required in many corporate governance codes. I do not expect any legislative activities on this point by the Commission, because I believe, this will be more or less regulated by the market.

A Shareholder Perspective:
David Pitt-Watson, Chief Executive, Hermes Focus Asset Management

I would like to focus on the public quoted company, which is, of course a European invention, I think the first one was the Dutch East India Company and the measurements and the processes that we use were of course an Italian invention, look at Patrioli who established the principles of accountancy. What the British brought to this was persuading the French Government in about 1720 to establish the Mississippi Company and thus created the greatest corporate scandal of all time. So, as a Brit, I am quite nervous addressing this.

I am also aware that that European invention some 400 years ago had quite a sticky start. To the degree that Adam Smith, in describing how he felt capitalism might work was very clear that the joint stock company had a very small part to play because he believed that 'negligence and confusion must always prevail more or less in the management of such a company where the management and the ownership have been separated the management will always take advantage of that position'. But, of course, as it turns out, Adam Smith was wrong and today's companies have become the engines of growth in our economies, indeed so far that James Wolfenson at the World Bank would say that corporate governance will be at least as important as national governance in the performance of economies going forward. So the goals of the company law action plan are not small in terms of the issues which they are trying to address. They are addressing the question of the structure of how we get those institutions which are going to be the engines of growth to deliver that and to do it in a way that protects shareholders and creditors and employees.

What then, in Europe, might we be trying to achieve? I would say, there are just 5 simple principles. First if we want our companies to be entrepreneurial, profitable and socially responsible, they have to be accountable. Where boards are elected or are clear where their remit lies, where there is independence, where shareholders or stakeholders have appropriate recourse through nominations, through extraordinary general meetings. In this we have taken enormous strides in terms of the accountability of companies, but much, much still needs to be done; much in terms of the nominations and how people become directors of companies, what qualifications they have for it; much in terms of share classes in term of voting, much to be done just in terms of simple mechanisms like share blocking that make this more difficult across Europe. But there is no point in just having accountable companies unless they are accountable to someone and to something so the first principle, accountable companies needs to be matched by responsible owners. Owners who are not just traders of shares. We need reforms in responsibility which are matching reforms in accountability. We need investors, particularly large institutional investors to start to acknowledge their responsibility, we need to have reporting of that responsibility. As Klaus Lehne said, we need to know who owns these big companies that is undertaking that influence and we need to participate as owners in those mechanisms that allow us to have influence. Again much as been done across Europe, but much still remains to be done. So accountable companies, responsible owners and we need relevant information about what companies are doing. It concerns me greatly that, over in the US, financial accounting standards boards would be telling us that the accounts are simply there to allow you to trade shares and do not need to include information on how you can become an owner. That is a huge step backwards. We need to have relevant, sensible information for the many millions of people who depend on the success of companies and we need the monitors and the people who are undertaking their roles and responsibilities to be fully independent that's the institutional shareholders, the accountants, the voting agencies. And we need a situation where society more generally, campaigners, trade unionists, whoever, have open access to companies, can talk to them and seek to influence them. Five very simple principles: accountable companies, responsible owners, relevant information, independent monitors and open access.

That forms the framework, but it doesn't offer a solution if you are a civil servant in Brussels because what I am talking about is not something that can be imposed by law. You can't say 'be a good company, be accountable, anyone who wants to get round laws that tell you to do that can do so, any investor that wants to cheat and sell shares and not undertake their responsibilities, they can do that.

So we can't legislate from Brussels, we probably can't even legislate at national government level. We need soft laws, professional standards. We need professional standards, we need understandings, we need owners to take responsibility as owners, we need ethics. We need an agreement on goals. I am stuck that, in the UK, we have had huge changes in Corporate Governance in the past 15 years, but it is only now that we are getting round to writing company law. The change came first, the law came second, not the other way round. And of course, if you try and impose a law on the many legal regimes that we have in Europe it will be a disaster.

The legal regimes, the soft law the institutions; you simply can't impose change from above. And add to that, not only do we have a local issue, but we have a global problem because 30 – 40% of European companies are actually owned by people who are not nationals of those countries. And given all of that, I imagine if you are a European civil servant, the idea of doing nothing must seem quite a good one. But that doesn't work either because if Europe doesn't take a stand on this there is a dominant model out there and it is an American model.

That American model of Corporate Governance isn't about ownership and accountability, it's about the integrity of capital markets, that is all it is about. It was put in place in 1933 because the states were responsible for company law and the only way, post the depression, that the government felt they could do anything about it was to regulate the capital market. We will have a set of regulations which will come to us globally, in Europe and throughout the world that comes from America that isn't based on accountability unless we decide what our principles are going to be here on this side of the Atlantic.

So how are we going to get there? We can see what the principles are, we know it can't be legislated for from Brussels. I think, what we need is a larger vision. A vision that must come from politicians and civil servants and we have them here and it is about the nature of the company and it's about the way in which capitalism is going to be successful and accountable. But is also about other people who are here, from stock exchanges, from standard setters who have soft regulation, which is probably couched in terms of comply or explain where you can break that legislation if you want to which fits in with the visions of the politicians.

Professional bodies also who are establishing what is your role if you are an accountant, who are you responsible to. Clarity of objectives in the boardrooms we have boards of directors, we have chairman at this meeting. Crucially investors and activists are effectively the representatives of beneficial owners. Campaigners and civil society groups and citizens and all of us, we all have to share a common vision each of us to play our part in that new European company and it's a huge agenda. It is absolutely about how we achieve prosperity because the governance of companies is as important to the world economy as the governments of countries.

At the beginning of the 21st century, 400 years after the Dutch East India Company, we have a new challenge for all of us in Europe to develop what is going to be the European model of the accountable company and to take this issues forward – all of us, not just legislators and I am delighted that we can be part of this conference where all of us can debate these issues.

Questions and Comments from the Floor:

Note: Questions were taken in batches of three and then answered by the panel.

Sir Nigel Wickes, Deputy Chairman,Euroclear SA. There's been a very great emphasis on the responsible shareholder and the responsible shareholder's needs to be able to vote his shares. In the last year or so it has become much easier for large UK investors to vote their shares, partly because my company, Crestco has allowed this to happen. There is no reason, in principle why some such system can't be generated across Europe. An investor fund based in Paris, ought, at the click of a button to be able to vote its shares in say a Spanish company. I very much hope the Commission is not just going to talk to lawyers about this but will talk to the people who will provide the systems that will allow this kind of voting to happen. At some stage someone will have to put in the infrastructure to allow this to happen.

Andre Baladi, Principal, Baladi and Associates. I was very impressed by the allusion to one share; one vote by Klaus Lehne. Can you develop what are the constraints? There are 44 major companies in Europe that have voting right caps: Novartis, 3%, Nestle etc. Why can't we have a voting right for everyone?

Mark Goyder, Director, Tomorrow's Company. It seems to me that the discussion this morning is taking place in a surreal context. Only one speaker mentioned Hedge Funds. We're talking about responsible ownership, our desire to see long term value creation at a time when it seems to me that the foundations of capital ownership are really shifting in a fundamental way. In the 19th Century capitalism was about family ownership, in the 20th Century it was about the principle and the agent, but I think you'd have to say in the 21st Century it is starting to be more about opaqueness, shifting ownership. Recently an American company said that they would have to break themselves up, not because they wanted to but because the pattern of share ownership they have – nearly 50% hedge funds dictates it to them. I would be interested to hear views on how we achieve a European model based on long-term value creation.

Panel Response:

Klaus Lehne: The Winter group delivered a proposal that was more or less taken on board by the Commission who later wanted one share; one vote in a takeover situation. But politics is all about interests and this means that there were many people who wanted exactly the opposite interest and wanted to keep their own voting rights. In the end we needed a qualified majority within the council and this was not possible to get at the time when we had to vote on the Takeover Directive and that is the simple answer to why we have not achieved this. What is now important, is that we simply have to go on and do some additional research, and maybe deliver another proposal that takes us more in that direction but we must not simply forget about it as it is a key problem between the different company law systems, and it is the job of the commission to keep going in this direction.

Anthony Burgmans: If you profess to be serving your shareholders, which shareholders do you mean. In the US the average flip time is seven months, so do I serve the shareholders who have my shares on average for seven months or those who have them for 7 years. This is a very important issue. There is not sufficient understanding in Europe when you say you serve your shareholders that they are serving everyone; people do not understand that if I buy back shares or give dividends, this cash usually goes to pension funds. And practically all of us are beneficiaries of pension funds. If we want to have policies that favour shareholders, we have to clarify this. At the moment the perception in parts of Europe, less so in the UK, but certainly in Germany and France is that shareholders are a small elitist group of people who control vast empires of wealth and whose interests do not coincide with the interests of society at large.

Questions and Comments from the floor:

Paul Dare, Retired: A question for Reiner Hoffman. Would you recommend to people that they be shareholders in European Companies and why.

Joelle Simon, French business confederation: I would like to react to Klaus Lehne. I fully support what he says about SMEs which represent 90% of European companies and I think we need a European legal form for SMEs. But I still have problems understanding why in liberal company law it is not possible to have different types of shares; single voting rights, multiple voting rights and also non-voting shares. Are you saying you want to ban non-voting shares?

Andrew Clearfield, Investment Initiatives, New York: I am concerned you are promoting a model of soft regulation which presumes that long term investors become actively involved in governance. Yet typically in Europe, the voting participation varies from 55% in the UK to about 25% or less on the continent. How can we have any kind of a regime which hopes to be self regulating in a situation where most of the structures actively discourage institutional shareholders, pension funds mostly, from voting shares and becoming involved in corporate governance. If you are going to depend on soft regulatory systems, then the legal obligations of the institutions that hold shares need to be better defined so that they are more or less compelled, or at least strongly encouraged to take an active role in governance.

Panel Response:

Reiner Hoffman: In many European member states, employees are shareholders. This is linked to the whole debate on financial participation. One crucial issue for us, as trade unions is that if we recommend that employees become shareholders, that this will not become mixed up with their salaries. But in general we think it is a good thing for employees to become shareholders because this means they have an interest in a solid and economically successful operation of the companies.

David Pitt Watson: I agree, you can't just have hard regulations or just have soft regulations or just have market solutions; you need all of these things. You need all of the people in this room to have a shared vision of what we are trying to create. I was intrigued by the comment from Euroclear; people will want to make money out of voting and they will put that in place. At Hermes, we are proud of what we have done, but we haven't done it because we are on a mission, we are trying to make as much money as we can for our investors by having better managed companies. But it needs to start with the vision. If we have accountable companies, then the rest will fall out.

Jean Pierre Hellebuyck: In response to Joelle Simon. We need to find ways to have holdings put in perspective. If you want longer term shareholders, you may want to have double voting rights for long-term holders. But of course, as investment managers are reluctant. Maybe in due course the market will make a difference because you will see that equities are out performing long term. If you hold equities more than 7 years, you have a chance to out perform. And so I would hope that the market will make a difference.

Klaus Lehne: I would be prepared to consider non-voting shares. We took them out of the discussion simply because they are different. The difference is that you would get a much higher dividend and therefore there is a price for giving up voting rights. But I agree they should be considered as part of the solutions.

Alan Johnson, Secretary of State for Trade & Industry, UK

In 1911, the President of Columbia University - Nicholas Butler - described the limited company as "the greatest single discovery of modern time", outweighing even electricity in its importance. Little did he know he was starting a debate that would still be raging a hundred years later. I won't arbitrate in that debate. But I will say that electricity and company law have both served us well in the last 150 years – keeping the lights and our enterprises switched on. Company law and corporate governance are vital to a successful economy. They can promote enterprise – or hold it back. Enhance competitiveness - or hinder it. They promote trust and confidence in our markets – so that people want to invest; do invest; and receive good returns on those investments. This matters to all of us. Not just as savers, pensioners or shareholders. But as workers, consumers and citizens too.

Today, I'm going to talk about our company law reform programme - at home and in Europe. But first I'd like to talk about the context of those reforms – the process of unprecedented change we are facing today in Europe.

The economic map of the world is changing like never before. India and China are producing more engineers, computer scientists and university graduates than Europe and America combined. Goldman Sachs predict that China's economy will outstrip America's by 2041. Technology is changing like never before. Products appear and disappear in the click of a mouse. Just ten years ago, there was no broadband, no video phones, no digital TV. The internet, text messages and DVDs were almost unheard of. Our demographics are changing like never before. In Europe, we have a falling birth rate - in many other countries it is rising. According to the UN, the population of Yemen could outstrip the population of Germany in fifty years. In the UK, the dependency ratio of workers to retirees was 14 to 1 in 1905, 4 to 1 now and will be 2 to 1 in 2050. By contrast, in India, 60% of the population is under 30! Change is constant. This presents huge challenges for European business, but enormous opportunities as well.

An opportunity to tap the Chinese and other rapidly developing markets. An opportunity to use our reach across the world. And an opportunity to sell our great ideas abroad.

Too often in Britain we take a glass half empty approach to globalisation. In response to the recent spate of foreign takeovers, some have said that our business is suffering "the Wimbledon effect". We can play host to the best competition in the world – but we can't win it. This is only half true. It is true that we play host to the international business community. The City of London is the financial capital of the world. Our science base is second to none. And English is the language of science, business and the internet.

But it is rubbish to say we can't win. Look at world beating companies like Vodafone, BP, HSBC, Smith and Nephew and Rolls Royce. The best companies in Britain are the best companies in the world. Overseas takeovers are a vote of confidence in our businesses - a sign of strength in our economy, rather than weakness. Overseas investment helps to stimulate competition and introduce innovation - bringing in new skills and processes. Like at Nissan Sunderland – now the most productive car plant in Europe.

The same is true in Europe. Historically our openness to other cultures has been key to our development. Bringing in new ideas, links with other cultures, and essential skills.

We need this diversity. In the UK and in Europe, the businesses that think global are the businesses that will succeed. And Governments have to think global as well.

It's an opportune time for the UK to hold both the Presidency of the European Union and of the G8, given that so many of the challenges we are facing need to be dealt with internationally. Europe is vital to Britain's prosperity. Over half our trade is with other EU member states. Millions of jobs are linked to that trade. Our ability to attract inward investment depends on our place in Europe. At Lisbon five years ago, all heads of Government agreed a strategy to make Europe the most competitive and dynamic knowledge based economy in the world. This represented a sea change in European thinking. It put competitiveness at the heart of our decision-making. Moving away from regulation to an approach based on enterprise, innovation and skills.

We are delighted the Barroso Commission has put such strong emphasis on economic reform. And it is encouraging that the Commission recognises how central company law and good corporate governance are to this. We need a corporate framework that promotes enterprise and encourages growth. That induces investment and supports employment. We need a framework that is flexible enough to adapt to different circumstances, but strong enough to hold directors to account. At a national level, these are the drivers behind the Company Law Reform Bill which we introduced into Parliament earlier this month. The Bill will bring savings to business of £250 million a year - £100 million to small businesses. It restructures the parts of company law that apply most to small business, making them easier to understand. It simplifies the way companies are formed; abolishes the need for company secretaries; and introduces new model articles. It means directors have to opt in to convening an annual general meeting, rather than opt out. It clarifies directors' duties; promotes electronic filing of accounts; and removes the need for hard copy share certificates. It also makes it easier for shareholders to hold companies to account. For example, by empowering them to put questions to auditors; requiring auditors to be named; and creating new offences of recklessly or knowingly including misleading, false or deceptive matters in an audit report.

Charlie McCreevy was right when he said that shareholders are the lifeblood of a company. Businesses work best where there is good communication and understanding between shareholders and managers. It's not enough for shareholders just to be informed about decisions. They need to understand them as well. Instead of making decisions for an immediate return, we need decisions that are made for the longer term. That's why we support the Commission's efforts to improve the exercise of shareholders rights across borders. A Shareholders Rights Directive has the potential to make a real difference. I look forward to seeing the Commission's proposals in due course.

More generally, the aims and principles that underpin the UK Company Law Reform Bill must also underpin our approach in Europe. That's why we welcomed the Commission Action Plan when it was first published in 2003. It provides a platform for fostering the efficiency and competitiveness of European business. Over the last few weeks we have been talking to other Member States about how the Action Plan should develop. As you would expect, there are differences on specifics, reflecting different national circumstances and traditions. But there is a lot of common ground. Strong support for the Commission's willingness to consult. Agreement that the focus of European action should be on dealing with cross-border issues. A desire to see clear strategic objectives for European action, focused on the need to promote competitiveness. And a wish for greater coherence both within this Action Plan and within the Financial Services Action Plan.

There is also a broad consensus that:

(i) any action should be based on flexible principles rather than a prescriptive rules based approach;

(ii) we should only intervene where there is clear evidence of a market failure; and

(iii) legislation should always be a last resort, and never our first reflex.

There is also support for the Commission's plans to simplify and modernise existing company law directives. Across the board, there is agreement that better regulation principles should lie at the heart of our approach. Better regulation means better policy. It means we can expect detailed roadmaps at the start; regulatory impact assessments as we proceed; and proper evaluations at the end.

Effective stakeholder engagement is key. To work, this must be a two way process. It requires the Commission to seek out stakeholder views. But it also requires stakeholders to engage with the Commission and national governments earlier.

These are important messages for this conference and the Commission's consultation which I know the Commissioner has very much taken on board. We will all need to reflect on these as we move forward. But we have a very positive and broad consensus to start from. Not just on the big issues about what we are trying to achieve. But the detail about how we move forward. This consensus bodes well. It gives us an excellent grounding to enhance our corporate governance framework. So our businesses perform better; our economies grow stronger; and our investments expand. This way we all stand to benefit.

Finally, in respect of the "Wimbledon effect" – yes, we're hosting the competition. But we are winning as well.

Report to the Plenary from the Breakout Sessions
Chaired by Pierre Delsaux.

The rapporteurs gave a short summary of each of the discussion groups, followed by brief comments from the chairs. This was followed by an open session with comments and questions from the floor.

Group 1 : Stakeholder Engagement

Chair: David Jackson, Company Secretary BP
Rapporteur: Colin Melvin, Director of Corporate Governance, Hermes

Question 1: What can/should the Commission do to improve engagement with stakeholders?
Question 2: What can/should stakeholders do to improve engagement with the Commission?
Question 3: How could stakeholders engage more effectively with each other?

Question 1: What can and should the Commission do to improve its engagement with the stakeholders?

There should be an improvement in communication and a better use of internet sites. There were some very negative comments about the Commission's own website and that of the DTI. More timely information and longer deadlines; give us enough time to respond is the message there, and some clarity on the Commission's role in relation to the consultations, and in relation to other stakeholders and what they believe the stakeholders' role is more generally about. Let us find, with the Commission, solutions to well-explained problems and not just take solutions off the peg from elsewhere. That was the first oblique reference to the introduction of US-style regulations in relation to governments within Europe, and that came back in again later on, somewhat more forcefully.
Clarity in the objective of the Commission; what is the Commission wanting us to do and what does it intend to do itself? More use of the Corporate Governance Forum; it exists, it's not being used effectively at the moment, we thought, and indeed of other advisory bodies at the Commission, and clarity on the process the Commission is following. Give us a roadmap, tell us what we're going to do next. Lastly, on this first question, some honesty about what is possible.

Question 2: What can and should the stakeholders do to improve engagement with the Commission?
It was felt by the group that to engage at all would be quite good! Far too many of the stakeholders in relation to Commission debates and consultations just are not participating. Where they are participating, this needs to be done early and at various levels. Stakeholders need to do their homework and back up their views. The

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Commission does spend some time itself doing background work, but, as stakeholders, we should be explaining in our responses to the Commission, the rationale behind our views to give evidence; evidence-based was the key phrase there. Stakeholders need to make constructive contributions. Don't just criticise, and be in a position to represent views more broadly, ie coordinate opinion amongst the various stakeholders rather than simply responding individually. Again, use the Corporate Governance Forum, the advisory body, and consider what the real issues are in terms of the future debate. Don't simply react to the short term communications with the Commission. Stakeholders need to think about where they want things to go and react accordingly. We noted the difficulties in lobbying and co-ordinating opinion. It's very costly, in terms of time and money, for individuals or individual institutions to lobby the Commission. Let us do so together and be more effective.

Question 3: How could stakeholders engage more effectively with each other? We already have existing business networks?
We had someone from the International Corporate Governance Network in this session, and she made a very good case for using the ICGN more effectively in relation to shareholders, but there are various other business networks and stakeholders need to look particularly to those that operate across jurisdictions, across boundaries and use those more effectively. Indeed, there may be a case for developing a new body for investors to engage with the Commission and other stakeholders, but particularly looking to the owners of companies, as David Pitt-Watson said earlier on today. Where are the owners of companies? Why are they not talking to each other? Why are they not coordinating their opinions? The big long term owners of our companies have broadly the same interests, they could quite easily, you would think, represent their views together. Perhaps there should be some sort of new body or mechanism for developing that and getting those views across. Indeed, these types of structures and bodies are a pre-condition and we consider that perhaps the third question needs to be answered first before we really engage with the other two. It is important to acknowledge the differences, the strengths and weaknesses in various regimes for constructive engagement. There are many good business practices around Europe. We have to look to those practices and make sure we capture them in our engagements with the Commission.

Finally, we had a brief and somewhat tetchy discussion about limiting the Commission's involvement in cross-border issues; perhaps the Commission should only be looking at those issues which are to do with cross-border-type themes, and not get so much involved in national government debates. The Commission, we felt, didn't properly understand and certainly wasn't projecting a common understanding of companies and company behaviour, and similarly employees and shareholders. A common theme which came out was don't simply pick up US-style governing structures and apply them to Europe, because they won't work here. We've got a far better system that we're developing ourselves. Lastly, make sure that you get the shareholders, the proper owners of companies, and involve them in debates.

David Jackson: There are a couple of things I would like to emphasize; two take aways. The first thing is clarity; clarity about what the intentions of the Commission are; about what the policy is; about what we're trying to achieve. Hopefully this new consultation on where the CLAP is going in future, will lead to clarity on policy. The second theme was, don't just think now, think for the future. We're trying to sort out corporate governance and company law to deal with the problems that have been in the past. But what about the future? Where are we going to be in five or ten years' time? What sort of company law and corporate governance system do we need for companies then. That's a bit of a difficult one for the politicians because there are probably not many votes in it, but certainly, I think for those of us who are involved in the system and who want to make corporate governance work that is what we ought to be focusing on.

Group Two: International Dimension

Chair: Barbara Thomas, Deputy Chairman, Financial Reporting Council
Rapporteur: Stephen Howaldt, CEO Hermes Focus Fund Asset Management Europe Ltd

Question 1: Is a global framework for corporate governance necessary or desirable?
Question 2: How do we get the US and other countries to interact with Europe?
Question 3: How should Europe operate in this area?

We considered all of the questions posed, but not necessarily in order.
We made a poll at the beginning of our group to just see how international the group actually was, because after all we are in the UK here and there was a risk it might be dominated by UK issues. We had 60 attendees and one-third were from the EU, but not from the UK, and another 10 were from outside of the EU. They all had their fair share of air time and I think we truly got an international dimension and debate. The overriding conclusion from all of this was that shareholders rights and effective corporate governance really went hand in hand, and you can only design good governance in a particular place if the shareholders rights actually match that system.

A delegate from Greece said, if there are any global principles they should be understood as a global language on corporate governance rather than hard and fast rules, so that if we do debate governance in the various countries, that we know what we are talking about. Some of the principles that were mentioned would apply on a global basis were that these should support enterprise, ensure accountability. There should be some procedure to address shareholder grievances, and there should, above all, be a duty on shareholders to vote, because obviously it's not just companies in these individual global places but also investors, many of whom invest abroad. Then, as we move to the EU, there was some understanding that shareholder rights and some convergence on shareholder rights was important. There was one contribution from the corporate world that said no, no, shareholder rights shouldn't converge, it's all about transparency. However, I think, as a group, some convergence of shareholder rights was seen as a positive. The local culture should be respected in doing so, and as one considers EU level rules rather than locals, it was mentioned that it could be quite burdensome, especially for cross-border investors, but also for companies, to respect all of the different codes that are in place across Europe. On the convergence of shareholder rights, it was mentioned that while this might be desirable, it might be wholly impossible, given the political realities in Europe. A contribution from outside the EU suggested that if we are to design something in terms of governance rules, one shouldn't ignore that the problems vary greatly whether you're in a closely held company or in a widely held company, and that the governance rules might have some differentiation to reflect this.

As far as cooperation by Europe with the US and others was concerned, it clearly focused on US and European cooperation and focussed on the fact that the US cannot be ignored because US investors already own a significant chunk of European companies. There is some spill over of US regulations as a consequence so it affects the way European business is done, and in particular it is relevant to focus on what investor government was in place outside Europe, especially in the US, and whether they had an obligation to vote and engage. There was also some agreement that the cooperation is not just won on the basis of governments and regulators, although regulators were commended for making a good start, but that investors, from time to time, would actually wish to coordinate but barriers are being built up to prevent that, and that was not very good. I think the final conclusion was that whatever is done don't just make it a lawyer's feast!

Barbara Thomas: I just wanted to add, that 20 years ago I wrote an article, when I was a Commissioner of the SEC in which I said, someday in America, men will turn on the radio and they'll listen to what's happened on the Tokyo stock exchange, and then they'll listen to what's happening on the London stock exchange, and then they'll go to work and look at their stocks. I got hate mail along the lines of 'Dear Commissioner Thomas, stick to your knitting, nobody cares about foreign securities, this is America, we have enough securities here'. Now 17% of American securities are owned by foreign owners, and we know that a number of Americans, including the dreaded hedge funds, own a lot of the European securities. So, the world is changing and we have to interact with each other, but we don't have to adopt other people's solutions. My one final thought about today in our session was that Europe has an opportunity to do it right. America's solution to its problems started in 1933 and 1934 with the Securities Acts, and maybe there was overreaction with Sarbanes Oxley, maybe they're thinking about it in America, but we don't have to react quickly and we don't have to overreact. The Commission is thinking about this in a very positive way, and this conference is a very positive response to that thought. Comply or explain work may translate very well across national boundaries, but certainly national boundaries are there to be respected as well as broad principles, and we have to take this as a real opportunity to get it right, so that 20 years from now, somebody won't tell a story like I did.

Group 3 : Accountability

Chair: Paul Myners, Chairman, Marks & Spencer
Rapporteur: John Leach, Managing Director, Hermes UK Focus Fund

Question 1: What should be the role of institutional shareholders?
Question 2: What more is required from companies?
Question 3: How far is legislation necessary to improve accountability?

John Leach: Of the three questions, I guess rather introspectively, we spent the majority of the time discussing question one and relatively little time discussing questions two or three which may be predictable. In respect of question one, what should be the role of institutional shareholders, we mainly spent the time talking about, firstly, communications and, secondly, appointments. In terms of communications, I think everyone believed in more dialogue, the main debate was how to facilitate that. There was a feeling that the routine results roadshows were not the answer. The dialogue should be more routine and not only occur when there was a problem. It was agreed that the opening up, in the UK particularly, of access to non-executive directors is a step in the right direction. But equally there was a feeling that fund managers should also address their own positions and there could be a greater convergence of the views of the investment experts and corporate governance people to provide corporates with a clearer message of what was required. We also debated what the nature of a long term investor was, bearing in mind the conversations that have been had earlier today regarding hedge funds and shorter term holders. We agreed that while hedge funds came and went, long-term holders remained and perhaps it was in their interests and also boards' interests to develop a two-way communication. As far as intervention was concerned, the dialogue was that it ought to stop at the boardroom door and that would satisfy the position between micro managing and macro influencing. There was a feeling that engagement was too much dominated by crisis and courage, or perhaps a lack of courage, in the absence of crisis. AGMs, was the one area of communication that we discussed in some detail and there was a feeling that institutions' reluctance to speak out at AGMs was a missed opportunity. We then discussed the extent to which institutions should be involved with appointments within a company; first the appointment of directors and second, notwithstanding what company law says, in practical terms, should shareholders be more involved in the appointment of auditors? As far as shareholders was concerned, and their directors, we had an interesting debate in that we had some representatives from the Swedish Corporate Governance body in the room, and we compared the norm in Sweden, where shareholders actively slating people for the Board, and the UK model. The room was split between those who felt that UK institutions should nominate directors to the Board and those who believed that would be a disaster. There was also a split between those who felt that communication through companies was done too much behind closed doors and those who felt it was definitely preferable that it was done behind closed doors. The one area that we didn't debate, which people might like to address later was voting records including whether voting records should be published, and if they were published should the institution have an obligation to write to companies with an explanation of negative votes and, indeed, whether they should give companies prior notice of negative votes at AGMs.

In terms of what more is required from companies, there was a general feeling that, moving on from current reporting requirements, institutions and companies could better communicate if there was greater information or dialogue on the strategic options and strategic plans of the companies. But most institutions in the room said they would be prepared to go inside to help debate with companies. Indeed, most of the time they were only going inside because of a lack of clarity about strategic options of the company. In terms of who the company is responsible to, again, there was a debate and I think they clarified that what we're really talking about is not what companies are responsible for, rather who are they responsible to. Indeed, they can only be responsible to shareholders as the utilisation of their risk capital.

In terms of legislation, there was a general feeling that legislation was generally not the preferred route in that it can be slow, cumbersome and hard to change and highlighted the benefits of soft legislation. In terms of addressing whether legislation was the only solution, there was some disagreement in the room in that some people felt that the current disclosure that we have on remuneration policies would not have happened without legislation. Another group felt that that legislation only came about because of shareholder pressure and there was a cause and effect debate there. Finally, on Pan-European, or UK legislation debate, again, I think there was a general feeling that we only really wanted Pan-European legislation where there were genuine cross-border issues to address.

Paul Myners: There are only really a couple of points I would add. Although we didn't take a poll in our group, I would estimate that it was probably 35-40% from the UK, 60% from outside the UK. What I think was more significant is the group was heavily weighted towards institutional investors and professional people involved in governance with a relative under-weighting of those from the corporate side of the debate. I think one of the questions we need to ask ourselves is whether we're making sufficient use of the powers that already exist, in particular, the obligations that lie on companies to produce annual report and accounts and regular reports in accordance with listing requirements. Are the institutional investors being active enough in specifying the type of things that they would expect to see covered? If we have a deficiency, for instance, on the vision statement, are institutions sufficiently honest to point out where they think the quality of reporting could be improved.

My final point is around the annual general meeting. AGMs empower shareholders in a pretty important way to propose candidates for election, to not vote in favour of candidates, to approve the election of auditors, and the opportunity to publicly voice concerns and issues. Until we put more regulatory burden on companies, we should first of all ask ourselves whether we're making sufficient, adequate and effective use of the obligations and arrangements which already exist to manage the interface between institutional owners and corporate managers.

Group 4 : Better Regulation

Chair: Sir David Arculus
Rapporteur: Tim Bush, Director, Hermes Focus Asset Management Fund

- Improving quality of consultation
- Improving processes for developing legislative proposals
- The Commission's approach to simplification of existing Company Law Directive

We started with a contribution from the Law Society who reminded us that law wasn't the only solution and that very often the Law Society recommends solutions other than law. It was felt that this was particularly important if you are trying to make law that effects different companies and that off the peg solutions do not necessarily suit the diversity in Europe. We then talked a little bit about consultations and the process of consultations. There was a view that consultations, almost by their nature, become rather self-selecting in that the people who tend to respond to consultations are those who were looking out for them in the first place and those that can afford to pay people to do the consultations.

There is a view that in some circles, that, in the last couple of years, it may have actually been more helpful to employ somebody in Brussels to lobby not to have consultations, rather than actually have to respond to the consultations which have been coming out, a comment on the volume of consultations over the last few years. There was a strong feeling that to have a new initiative you should really be demonstrating market failure and only when there is a clear market failure should there be a cause for legislation. There was also a sense of joining up within the EU that felt that there's been a silo approach with different bits dealing with broadly the same thing. This manifested itself with company law experts appearing to be somewhat overridden by initiatives coming out of capital markets over the last two or three years, creating some tension. It was also felt that perhaps there should be a scope rule within the European Parliament so that legislative proposals stick to the original policy agenda and don't develop a life of their own with mission creep. So, we felt that there was a risk of ending up with something worse than we started out with. One person commented that maximum harmonisation objectives could become straightjackets. We had a debate about the length of the consultations and time scales; the minimum standard is eight weeks and if representative bodies themselves are going to have to consult, this is too short. Interesting views from Company's House who looked at users and not regulators' requirements and recognises that regulation might not actually add value. A strong sense that even if we are talking about governance by codes, we should remember that the primary purpose of business is to generate value. Stock lending was a good example where regulation could be tidied up by market best practice. As someone said 'The internet didn't happen because of a committee.' The UK Shareholder Association actually threw up what, for many people, is a new issue in terms of the disenfranchisement of smaller shareholders in nominee accounts. And, again, there was an interesting view here, that rather than legislating the Government may actually assist markets to come up with solutions, and a good model of that we had was the Myners' review that actually shone a light on the problem rather than actually proposing prescriptive legislation at the outset. So, I think we concluded that pre-consultations might be a solution rather than full consultations.

David Arculus: In our group there was a strong bias towards soft law, to alternatives to regulation. I think there was a bias to thinking about policies not about regulation. Let's consider how we can achieve things as opposed to getting hung up in the regulatory process. I would say over 50% of our time was spent talking about consultation, and the various models for consultation. I think the general opinion was that we need to use them all. We need groups of experts, we need internet consultation, we need as many kinds of consultation as we can get, and over as long a period as possible, and a representative from UNICE pointed out that it was impossible to consult with all their members and all their member organisations and then collate all the opinions within a short time period like eight weeks and so we did need to have a lot of extension there. As far as alternatives to regulation are concerned, they are obviously much more flexible than regulation and I think there is a great future in terms of soft law and alternatives to what you might call classic regulation, and we would commend that to people. The final comment which is based on my own experience, I think the more you regulate the less you tend to get of things. When you look at something like Sarbanes Oxley in the US, you see a process now of companies starting to deregister from the SEC. So, the whole issue of what is the right level of regulation for Europe and perhaps having some competitive regulation compared to other territories in the world, I think is an interesting idea that might be developed further.

Questions and Comments from the floor

Peter Montagnon, Association of British Insurers: I'd like to come back to the first subject which was about engaging with the Commission. We engage with the Commission and figure out with them what needs to be done, and then the whole thing moves into the Parliament and becomes unpicked. Perhaps someone from the group, or Pierre, you yourself, might give us some sort of insight into how can we bring the Parliament into the process so that it really is joined up all the way along?

Ken Rushton, a former regulator: One reason why you might be hearing a lot of push-back in favour of soft law over regulation is the ever increasing tendency of the Commission to be over-elaborative in regulations. When consultation papers come out, there are very seductive words about framework directives, principles based regulation, but inevitably it seems that the result of pressures from I don't know where, I don't think it's the responses to the consultation, it may be the fact there are so many member States, the regulation itself becomes evermore detailed and evermore complex, and that is the problem. If you could resist that temptation and stick at the basis of principles, there might actually be more support for Commission regulation and less for soft law. But while you're so elaborate and you're so detailed I don't think you'll get that support.

Pierre Delsaux: There is a link between this question and the first one because the Commission made the proposal but obviously the Parliament and the member States which are also involved in the process of finalising the text at community level.

David Arculus: It is fair to say that the whole question of the Parliament was raised in our group and the way we tried to solve it was to try and get consensus about what the policy is and what we're trying to achieve first, i.e. to have some sort of pre-consultation about policy before we actually got into the legislation side of it. That was our answer, but I don't know whether Pierre, from his experience, has other thoughts.

Pierre Delsaux: On this particular question, and clearly as you know, the Commission makes a proposal, a good proposal sometimes, but then this is discussed by 25 Member States and the Parliament. When the Commission is supposed to make the proposal we will have a full consultation process, we'll have an impact assessment and we will try to evaluate the consequences of our proposal. When we have made this proposal and we start the legislative process with Parliament and consult the Member States, even if the same requirements are being enforced on the Member States and the Parliament and you can have some important modifications of the Commission's proposal being made by the Member States or by the Parliament without a full impact assessment or even a limited impact assessment. One way we are exploring and we know it's politically sensitive would be at least to request from the Member States and from the Parliament when they make a substantial modification of the Commission's proposal, to at least provide the other member states and the Commission with some kind of at least limited impact assessment of the consequences of the proposal. I agree with you. At the end of the day you might have a proposal which, at the start, a principle based proposal, but at end of the process it becomes something which is very complicated, and sometimes very difficult to read, sometimes barely understandable for anybody, even for those involved in the negotiations. So, clearly we need to change that because I agree with you, and the quality of legislation is also fundamental if you want it to be accepted by the business community and other stakeholders, and that's what we want because legislation which is not being applied or is not understood or accepted by the business community, is a useless exercise. But it's a difficult question and, except maybe requesting from the Member State and the Parliament some kind of impact assessment once they make modifications to the proposal, I don't see how we can solve this issue because obviously you are an independent of the Parliament, independent of the Member State, you should be free to decide.

On the second question on the hedge funds, who would like to respond to this question?

Jonathon Rickford, British Institute of International and Comparative Law: Can I make a comment on that and on the proposal from the first group on imposing their fiduciary duty on institutional investors to vote. There are company managements who have a vested interest against change. There are Member State Governments who have a vested interest against change. I can think of two good ways of supporting those two lobby groups. One would be to disenfranchise short term shareholders to say that before a shareholder can vote he must have shown loyalty to a company for a certain period of time. Another way of supporting those vested interests would be to say, we'll impose an obligation on all institutional investors to vote, or we'll reward them for voting. What will the affect of those two proposals be? We will create a liquid and sticky market and corporate control because we will have a higher cost in acquiring control of companies as a result of the delay which is built in to a process which penalises short term shareholders. And we will create a situation where we have an incentive to people who don't know what they think, to vote and, of course, if they don't know what they think, they'll vote in support of management. Now, if I can revert for a moment to the wicked hedge funds. The hedge funds have exactly the same stake in a company if they hold shares as any other shareholder. I have the same stake in the company if I bought my share 15 years ago and propose not to sell, as I have as if I bought it yesterday and proposed to sell it tomorrow. If we penalise people for selling, then we will penalise people for being active in the views of the performance of businesses. A good example is Deutsche Borse, where shareholders, some of them short term and some of them long term, took a view about the prospects for the company which would result from a strategy that was proposed by the existing management; they took a rational view of what the impact would be on their pockets in terms of the destruction of value or the creation of value of the strategy that Deutsche Borse adopted. So, let's be very, very careful about this fallacy of treating a person who is going to sell tomorrow as different

Mark Goyder, Tomorrow's Company: Having raised the issue of hedge funds this morning I would like to react because I think Jonathan Rickford's elegant academic arguments actually miss some heavy reality. What we used to see is two disciplines on companies. One was about the discipline of, and always has been about the discipline of the share price and the other was about the discipline of ownership and accountability, and the reason why we're raising this issue about hedge funds is not because there is some generalised value judgement being made about hedge funds being bad or other institutional investors being good, it is simply objectively to observe that we are seeing an erosion of the discipline of ownership and that would leave capitalism in a curious situation where the only discipline of it was the discipline of the share price, which certainly leads to very different behaviours. I think we need to think about those implications.

Peter Butler, Governance for Owners: This short term, long term debate is very important and the difficulty is that the short term holders, the hedge funds, seem to have become more powerful in the market recently, and yet probably they're in a minority. The reasons is that the markets are reacting to create this large amount of value and the opportunity to get involved by hedge funds, whereas at the long term end of the market, the owners are not accepting their responsibilities, and there is no market mechanism that encourages them to do so. My solution to this is that if you hold a share for more than a certain amount of time, and one can argue how long that should be, let's say two years, then a small additional dividend should be paid and that, of course, goes away when the share is sold so it doesn't distort the market price of the share. But what it does do is it provides a small amount of additional income to the long-term share owner so that, perhaps, they will think a little more about exercising their ownership rights and encourage them to think harder before lending stock to the short term end of the market and the damaging consequences that can bring.

Alan Macdougall, PIRC: I want to say three things about hedge funds. It seems to me that hedge funds are trying to persuade the market that they don't need a level of regulation that all other asset management vehicles have to go through, and there's a danger here that the financial regulators will let them off the hook. I think, for investors, long term or short term, a particular section of the market should not have the privilege of less transparency about the way they operate than others. The second thing is that in very few cases do we know what the stated strategy of these hedge fund operators is, vis-à-vis, particular shares. I think one of the transparencies about most asset managers who manage pension fund assets for the long term is that they are clear about their strategies and, broadly speaking, there is a consensus in the marketplace about what they're trying to do, so there is less fear on the corporate side about engaging with them. The third issue is the question of cost and what do pension fund trustees do? A lot of pension fund trustees, many represented in this room, have recently gone into hedge funds for the first time; I think those trustees ought to be more accountable for the investments they make in hedge funds to the other companies they are invested in; investors and trustees in this case have to be much more transparent about why they're making these decisions to invest in hedge fund vehicles. Finally, to quote President Pompidou on losing money. 'The quickest way to lose money is through the horses, the most pleasant way to lose money is with the opposite sex and the most certain way to lose money is to take the advice of financial experts.' I'd like to add a fourth one; the most expensive way to lose money is to invest in hedge funds!

Jon Lukomnik, Sinclair Capital, US: I normally wouldn't speak in a public forum in Europe on hedge funds, but I have run a top 10 pension fund globally for the New York City Pension Funds. I've been managing director of a top 10 hedge fund, I've recently worked for a number of hedge funds. People are speaking about hedge funds as if they are monolithic. They are not. You're saying they're short termism. The last hedge fund I worked for was ESL, Eddie Lampert which has become a major majority owner of Sears and his average holding period is well over five years. I find it highly ironic that there is a discussion about short termism on hedge funds here when what people seem to be annoyed about is that hedge funds are doing exactly what they're supposed to do which is acting as owners. People only seem to be involved and annoyed when they hold people to account, whether it is the Deutsche Borse or elsewhere. There are short term trading hedge funds. I suspect people here really don't care about them because they don't vote and don't get involved, and the hedge funds that people seem to be annoyed about is because they are something new and not understood, and therefore a challenge to the status quo by doing exactly what everyone in this room would like which is engaging and being activist owners. So, the one thing I would urge the Commission, is whatever you do regarding hedge funds, and I'm not saying they shouldn't be regulated the way other financial institutions are, but, please, they are every bit as multi-varied and dispersed and diverse as other holders. There are activists, there are people who will hold your stocks for 15 seconds, not just days, but they also are often some of the most intelligent investors you will have who can take large stakes and therefore try to understand your company more than, for instance, an index fund manager, and there are also those that are unintelligent and really will look for a short term pop, and so please be aware that this discussion of hedge funds is akin to someone who's familiar with hedge funds as if saying, I can't distinguish between French people because they all sound alike. It is equally xenophobic, equally wrong and you really need a level of discrimination that I'm surprised has not been here.

David Doyle, ACCA: I'd like to raise something unrelated to this hedge fund issue and this is a question of enforcement of regulation. Building confidence in a single capital market in Europe is not just about good regulations or better regulations it's also about ensuring robust enforcement, of course, you are 25 Member States. It seems to me that we have a lot of evidence showing that there is enormous fragmentation and divergence of enforcement mechanisms across Europe. I think this has to be addressed for two reasons. One because we find in every aspect of the financial services action plan, that there are different interpretations given to various directives and bits of regulations and, secondly, there is a good possibility, a good risk actually, of duplication of enforcement mechanisms both within the national States and at the European level. I would suggest that some careful consideration and quality thinking needs to be given to enforcement of regulation if we are to build up confidence in the capital markets.

Pierre Delsaux: That's not a new priority for the Commission. You might have seen the Green Paper and the White Paper on financial services action plan and clearly the one message in these two documents is clearly enforcement is a priority, there should be appropriate mechanisms to be sure that enforcement for equal level, everyone in the community and we should also find mechanisms to be sure that too much enforcement creating problems because of too many enforcers being responsible for the same plan. But I note your comment.

The following comments were submitted by delegates after the conference:

Lucy Jones, Private investor and corporate governance researcher and David Dodson private investor and lecturer, City University, London

Stakeholder engagement at corporate governance level requires ‘empowering’ stakeholders. Specifically, stakeholders need appropriate ease of access to public information (such as company announcements) and appropriate opportunities to influence companies.
Important opportunities to influence companies may involve communicating concerns to shareholders and having shareholders empowered to influence company boards, aside from whether there is a unitary or two-tier board.
Also, risk analysis in company reports should perhaps include at least recognition of all known stakeholder opposition to company plans or actions.

Stakeholders can improve engagement with companies, and with each other, among other things, by being active shareholders, by appropriate empowerment of shareholders, and through more widespread public understanding of business ethics (see e.g. Crane and Matten, “Business Ethics - A European Perspective”, 2004).

We see empowerment of shareholders as the core issue.
They are the owners of companies but too often directors do not serve their interests well.

Shareholder empowerment requires giving shareholders appropriate ease of access to information (e.g. web access to full recordings of investor briefings?), appropriate opportunities to communicate concerns to directors and appropriate control over company boards.

The UK Shareholder Association makes many important points regarding shareholder empowerment. In particular we agree that board remuneration should be confined within limits approved by shareholders in advance.

We also worry about director’s motivation, particularly where their long term financial interests are not well aligned with long term shareholder interests.
In particular we fear that promoting independence of non-executive directors all too often encourages them to act in their own interests while expressing conventional rhetoric about serving shareholders.

We thus feel that director’s annual remuneration should include a significant element of shareholding in the company, held in trust and not released to them for several years, unless they already have such a trust investment significant in relation to their wealth.
Martin Morton, Committee Member of the United Kingdom Shareholders Association, (UKSA):

1.The role of the institutional shareholder. They have resources that individual or even groups of private shareholders do not have. They must take account not only of the macro

issues but also be aware of the investing problems of the smaller shareholders. When the concern of smaller shareholder over their disenfranchisement when forced into nominee holdings was raised this was described as “a new and interesting point of concern”.
It is not new. UKSA has been complaining about this for several years.
Smaller shareholders, and especially investors in ISAs. and PEPs. are forced into this situation quite unnecessarily. When the institutions comment, favourably or unfavourably, on a company, their views should normally be made public. They should be expected to raise concerns openly at AGMs.

2. The role of the non-executive director is pivotal. They are not there to bolster the Chairman whose friend they have often been in the past. They have a significant role in representing the shareholders to the extent of challenging, if not removing, the executive directors for serious management failure. Where necessary they should consider resigning to make their point, even if sometimes they are the only one making it. Some companies are critical of the conduct of the AGM, and their cost. It is frequently a social meeting place for former employees who are shareholders, or for one issue campaigners, or both. They should be an occasion for a serious debate on the progress and future of the company. This is difficult to stage manage without becoming artificial, but consideration should be widely given to making it more of a reality.

3. The role of legislation. There is probably too much legislation which often inhibits initiative, but if companies do not “comply or explain” in relation to codes, then legislation is inevitable. Companies should not wait for commentators to discover they are not recognising codes, but should explain up front what they are going to do outside their provisions, and why. There may well be good reasons that would not be admissible under legislation. The Remuneration Report which all now consider important would not have been adopted by most companies if it had not been made a legal requirement.

The EU Corporate Governance Forum

The Forum and its work: Gerhard Cromme, Chairman of Supervisory Board, ThyssenKrupp

First the corporate governance trends in the European Union. The EU Commission continues to work consistently on the implementation of its corporate governance action plan of May 21st 2003 on the modernisation of company law and enhancement of corporate governance in the European Union. This action plan is based largely on the findings of the high level group of company law experts headed by Professor Jaap Winter. Many themes of the action plan have met with approval in the EU member states. This is true for most of the European countries.

The fundamental idea is to promote the convergence of corporate governance of European companies. However, given the diversity of current practice, a standard corporate governance code for Europe cannot be the solution. Europe needs standardised principles for the key aspect but not standardised rules of law. There are considerable differences between the countries: their leader systems, their ownership structures, financial tradition and corporate culture. These differences must not be underestimated because they are reflected in the corporate governance practices of the individual countries. National corporate governance codes which are based on common fundamental principles, but which take into account national peculiarities, are therefore the best way to improve corporate governance in Europe.

To understand these national peculiarities it is important to look at the social and historical parameters, together with the corporate and capital market laws which ultimately influence the impact of shareholder structure. For modern day shareholder structures it is of decisive importance whether companies in specific countries have been financed in the past, for instance, more from borrowed capital, pension fund or equity capital. The bank which provides the loan is different from the fund or broad based shareholder investment.

Last, but not least, corporate governance systems are influenced by the different shareholder structures. In the end different shareholders have different expectations with regard to their companies. The national differences increase further in number if other stakeholders such as employees, customers and the general public are taken into consideration for matters of corporate governance. An objective discussion on corporate governance can only take place in the knowledge of these differences. Unfortunately, matters are often made more difficult by ill considered general adoption of English terms as bad words in other Governance systems. When complicated terms and legal concepts are equated for the sake of simplification misunderstandings are inevitable and discussion is often taken in the wrong direction.

To illustrate this, I would like to use the example of the one-tier and two-tier management system.

The one-tier system with one board comprising executive and non-executive directors is in many ways not comparable with the two-tier system comprising two separate boards, executive and supervisory with distinctly different tasks. In the one-tier system the board manages all business and, at the same time, is responsible for its oversight. In the two-tier system the management board tenders business by the supervisory board, provides advice and oversees its activities. The distinction of executive and non-executive for outside directors within a single body no doubt makes it possible to separate the management and supervision functions within the board. However, this is not the same as institutional separation of the two areas as defined on the Continent in Europe. The chairman in the one-tier system is not the same as the supervisory board chairman because the chairman in the one-tier system frequently also bears responsibility for the operating business. A management board member cannot at the same time be a member of the supervisory board whereas the functions of CEO and chairman are frequently performed by one and the same person, particularly in the US and in France. The German and Continental two-tier system with management board and supervisory board provides for a clear separation of the two roles and establishes - if it is well implemented naturally - the desired system of checks and balances.

In Germany, unfortunately, this clear separation of responsibilities is overshadowed by the role of the workers' representatives on the supervisory board through co-determination. But it doesn't change the principle of the clear separation of the role of the management and the supervisory board. By contrast in the US, where the board positions of chairman and CEO are frequently held by a single person, conflicts of opinion are, figuratively speaking, merged in one person. The undisputed advantage of this system is that decisions are made more quickly but the lack of institutionalised debate is a serious disadvantage. Attempts are being made on the Continent to strengthen cooperation between the management board and the supervisory board and to strengthen the role of the supervisory board, for example, by intensifying committee work. In the US and in the UK, efforts are underway to underline the independence of non-executive directors and, in the UK, to separate the roles of CEO and chairman.

Knowledge of all these differences – and I'm just mentioning a few – is necessary if we are to discuss individual corporate governance issues objectively in Europe and make an appropriate assessment of the, in part, differential practical solutions. Developing general transmission principles on the basis of this insight and thereby contributing to the convergence of European corporate governance codes at a practical level is the key task of the European Corporate Governance Forum.

Ladies and Gentlemen, the European Corporate Governance Forum is an initiative of the European Commission. The establishment of the Forum was one of the short term measures specified in the Action Plan; it was created by the Commission's decision of October 15th 2004.

The Forum comprises 15 members who were selected by the EU Commission on the basis of their experience and knowledge of corporate governance. Members of the Forum are each appointed for a period of three years. The Forum is chaired by a representative of the EU Commission; the office is currently held by Alexander Schaub, Director-General for the Internal Market and Services. It is the shared understanding of the EU Commission and members of the Forum that the Forum's work is independent of the Commission's specifications. The Forum organises its own work, identifies key themes and publishes its deliberations. The Forum is represented externally by a spokesman. At the first meeting of the Forum the members unanimously elected Bertrand Collumb, Chairman of Lafarge, as their spokesman, and I'm confident and sure that we made a very good decision. So far the Forum has had two meetings. The first meeting was on 20th January 2005 and the second meeting was on 20th June 2005 and we will meet next Monday again in Brussels. Our minutes are recorded and published on the website of the EU Commission.

In the meetings of the Forum an intensive exchange of minds takes place on current corporate governance topics. This brings me to the tasks and objectives of the Forum which are described in the closing report of the Winter Group and in the Action Plan of the EU Commission and which are specified in more detail in the Commission's decision of 15th October 2004. According to the decision, the aim of the Forum is to enhance the quality of national corporate governance codes and supervise strategic advice to the Commission on corporate governance. This ultimately is what distinguishes the European Forum from the group of non-governmental experts on corporate governance and company law whose task is to provide expert support to the Commission on draft legislation.

Fortunately it's not the Forum's task to develop a European corporate governance code because on this matter there is a general consensus among all of us that the development of the standard code would be doomed to failure from the outset. I have already mentioned and explained the reasons for this. On the basis of the legal conditions prevailing in the individual EU member states the European corporate governance Forum will discuss views and perspectives at European level in an effort to develop common principles of good corporate governance which takes into account the different conditions. What are the current discussion themes of the Forum?

The Forum has identified three themes which are initial priorities. These are the Comply or Explain mechanism, the companies' internal control and risk management system and the role of the stockholder.

We will deal intensively with the Comply or Explain principle in the Forum. The main question here is how this principle, which features prominently in corporate governance codes, is applied in the individual member countries. In concrete terms we will investigate, for example, how observance of the Comply or Explain requirement is monitored and whether enforcement measures might possibly be required. Ultimately we will have to discuss cross-border methods in this context. My colleague, Peter Montagnon, sitting next to me, will be looking at these extremely interesting aspects of Comply or Explain in more detail in a moment.

As far as internal control and risk management is concerned, here the Forum is addressing the question of what internal control systems are needed to prevent accounting scandals such as those we witnessed over the last years. It appears questionable to me that the cost intensive control system implemented by the Sarbanes-Oxley Act in the US can serve as a model. There are positive signs and there are negative signs. Forthcoming measures at European level, and in particular the amendment of the Eighth Directive, the so-called Auditing Directive, will lead to considerable improvements. Jaap Winter will be outlining the Forum's deliberations on internal controls and risk management later.

As regards the role of the stockholders, in 2004 and in 2005 the EU Commission conducted two public consultations on the role of stockholders in the corporate governance systems of the member states. The Commission presented the findings of the survey to the Forum. In the discussions it was agreed that an EU Directive on the role and rights of stockholders is expedient. However, in view of the existing national differences in the scope of stockholder rights, the directive should set out basic principles rather than contain detailed provisions. The aim should be to facilitate the exercise of stockholder rights at Annual General Meetings and thus help increase the involvement of stockholders in major company decisions. Binding European rules on the exercise of voting rights across borders may help here.

A Europe wide standardisation of stockholder rights exchanged with the companies is not considered expedient by the Forum. Nevertheless, to prepare for further discussion it maybe helpful to obtain information on the role of stockholders in the individual countries, Alastair Ross Goobey and Antonio Borges will be reporting on this and other considerations of the Forum in a moment.

Comply or Explain:
Peter Montagnon, Head of Investment Affairs, Association of British Insurers

It's a great pleasure to be here and to talk to this conference about the principle of comply or explain – but I feel at the outset a need to give a few words of *explanation* myself.

Insofar as the billing suggests I am going to talk to you about the work of the Forum in this area, I cannot really comply as the Forum has so far completed no work on comply-or-explain. We were due to have a discussion of the subject in the summer but for reasons of time and, given the other pressing matters on the agenda, we decided to defer this until our next meeting in a week's time. There are therefore, as of now, no conclusions on which to report. I hope you will therefore accept this explanation without imposing regulatory sanction. But there is still general recognition that this is an important subject for the Forum to consider. Rather than trying to report about work that has not yet been done, I will attempt an alternative - to set out some of the factors we will need to take into account as we prepare to address the subject.

In doing so I have to be clear that I am speaking in a personal capacity rather than on behalf of the Forum, which as I have explained has formed no conclusions yet. My locus for doing so is that I have prepared a paper for the Forum, but it is a discussion paper with only tentative conclusions rather than a consensus document. We will have to have some pretty intense discussion of the issues because, while the concept of comply-or-explain is well understood in the UK, it appears less obviously workable as an approach when you start to look at what happens elsewhere in Europe. The Forum will have to take account of the fact that there are some real constraints, and that, even if we wanted to, we cannot simply expect to set a timetable for rolling out the UK approach across all member states. On the other hand, we in the UK have found that there are clear advantages to using a code-based comply-or-explain approach as an alternative to regulation. It ought to be beneficial, if Europe, as a whole, could reap the maximum benefit from this UK experience.

So what I want to do today is to try to set the scene for the debate we are going to have, looking first of all at the concept of comply-or-explain and then set that against the key considerations at the European level. There are some pretty big questions here. Can comply or explain work in markets where the ownership structures are different to the diversified portfolio pattern we see in the UK? Can it work if shareholder rights are inadequate to the task? What sort of issues require a legislative or regulatory approach and what can be left to a Code? How exactly should the law interface with the "voluntary" approach? How far is there a need for a common European legal approach, and how far can member states develop their own solutions, given that they are coming from a wide range of starting points? As part of our effort to raise standards of corporate governance across the European Union we need to consider all of these questions. Though I can't give you any firm conclusions today, I believe the input we receive from you, the delegates to this conference, will also help inform our discussion. So my aim is to keep this speech reasonably short and leave plenty of time for you to air your views after I have finished.

I will divide my remarks into four basic parts. First, I want to make some philosophical remarks about the value of comply-or-explain as an approach. Second, I will look at the UK experience and seek to pinpoint the factors that make it work. Third, I will draw on this to flesh out in a little more detail the constraints facing the rest of Europe. Fourth I will draw some tentative conclusions about how Europe might approach the challenge.

One of the big myths promulgated about comply or explain by those who do not understand it well is that it is self-regulation. This would be true if it led to companies deciding for themselves whether they should comply with the provisions of a code. In fact they can deviate from the code, but only if they produce an explanation which satisfies the shareholders who own them. In other words this is not self-regulation but a system whereby companies are held *accountable* not to a regulator or other public authority but to *shareholders*.

It is possible to operate such a system in the UK because shareholders here have real rights – they can appoint and dismiss directors. It is worth dwelling for a moment on this point and contrasting it with what happens in the US where shareholders do not possess this crucial right. Because of this US companies and the boards that run them are not ultimately accountable to their owners and the only party to whom they can be accountable are the regulatory authorities. This is why, in the wake the corporate scandals that hit the US around the turn of the century, the US had to resort to highly prescriptive, cumbersome, rigid and expensive legislation. The UK chose in contrast to review and strengthen its corporate governance code, including separate specific efforts to examine the role of audit committees and the way boards approach the question of internal controls.

Look at the result for one of the key areas of governance - internal controls. In the US, the Sarbanes-Oxley act requires executives to certify the effectiveness of internal controls. The cost of compliance and the necessary verification runs to tens or hundreds of millions of dollars. The result has been disclosures, which in some cases have forced boards to tighten up procedures. But in the UK a broadly similar result in terms of outcome has been achieved by the voluntary Turnbull Guidance which simply calls on companies to confirm in their annual reports that their boards have reviewed internal controls. The Turnbull Guidance has been reviewed this year and the conclusion, supported by investors as well as companies, was that there was no need for radical change because the mere fact that boards have been disclosing that they have undertaken a review has caused them to take risk management much more seriously with a real behavioural change. This change has of course been achieved at vastly lower compliance cost than in the US.

The key lesson here is that a code-based comply-or-explain approach is an alternative to intrusive regulation. There is an opportunity for Europe to build on this to create a regulatory system that is effective and vastly less expensive than that of the US. Why, after all, should we in Europe presume that what comes out of the US must be best? It could, and perhaps should, be argued that Europe can do better than the US and avoid the mistakes that country made with its over hasty reaction to corporate scandals in the form of Sarbanes-Oxley.

But it will not be easy. There remains a big question about how suited this approach is to Europe as a whole. I want to address that first by looking briefly at the UK experience, trying to single out the factors that make it effective and seeing whether they are present elsewhere in the Union.

In Britain, we have had over a decade of experience with codes, starting with the Cadbury Code of 1992 and building up to last year's Higgs Code. The Code, as I noted earlier, is not regulation but a statement, agreed by both investors and companies of what constitutes best practice. Because it has a consensual basis, there is peer pressure to conform, but where companies feel they have specific reasons for not applying its provisions they are able to explain why they have chosen to deviate. Provided shareholders accept the justification, this is an end of the matter.

Successive codes have been successful in raising standards and driving change over time. For example, the roles of chairman and chief executive were frequently combined when the Cadbury Code was introduced, but this is now highly exceptional. UK-listed companies generally have a well-developed board committee structure with a generally good balance of executive and independent non-executive directors. Audit committees and remuneration committees function well without the need for specific regulation. A more recent example of change is that most boards nowadays undertake some form of performance evaluation, which is provided for in the UK code. A few years ago, the idea of performance evaluation for directors would have been unthinkable.

So the UK approach can substitute effectively for more formal regulation, though it is important to remember that not everything can be handled in this way. It is also important to ask what are the factors that make the UK approach work, as this will shed light on the possibility of adapting it to the rest of Europe. There are three main factors behind successful implementation: buy-in to the basic principles by the whole market, a high level of transparency and a real prospect of sanction for those who refuse to conform without adequate explanation. In the UK, as I have already mentioned, the sanction is that the shareholders have the ultimate right to dismiss the board.

Now it is necessary to ask whether these factors come together so that they can be similarly put to work in other European markets. The short answer is that it is a pretty difficult prospect. For a start, the UK approach works not only because UK holders have the right to appoint and dismiss boards but also because the prevalence of portfolio investment means the ownership structure is pretty well diversified.

I asked my colleagues to dig out some figures on this and they are pretty revealing. Whereas in the UK collective investors like insurance companies, pension funds and mutual funds hold just over 50 per cent of the market, elsewhere in Europe the figure is much lower. In Germany it is only 18 per cent. But in contrast non-financial private enterprises hold around 40 per cent of the market in Germany, compared with only 3.5 per cent in the UK. A similar pattern occurs elsewhere with the proportion of non-financial private enterprises being high relative to collective investment.

The figure for non-financial enterprises is a very rough proxy for strategic industrial holdings, which are often of a blocking nature. What the figures point to therefore is a situation where many European markets have a rather concentrated ownership structure in which leading shareholders may be close to the management and the real minority shareholders rather weak. This means there may not be enough independent shareholders to make the accountability process work properly. In these markets regulators are bound to be a bit more sceptical even if the shareholders do have the right to appoint and dismiss boards. On top of that the real rights of shareholders are weakened in a number of countries by distortions of voting rights, like voting ceilings, multiple voting rights and depositary receipts. So it is small wonder that regulators are sometimes sceptical of what comply or explain can achieve in their own national markets.

One of the other challenges facing continental European markets in developing a comply-or-explain approach is that it is not always easy for the authorities to understand the UK's ability to place issues affecting financial markets somewhere in the middle ground between statute and voluntary good behaviour. Until the Takeover Directive came along, for example, the Takeover Panel operated effectively on a non-statutory basis. Reporting under the Combined Code is a requirement under the Listing Rules, but this too was in the hands of the Stock Exchange until demutualization, and even now the Financial Services Authority operates a light-touch regime. In most European markets there is a desire for greater certainty about what is a statutory requirement or a regulation that can be enforced and what is simply best practice. There is a lack of willingness to create hybrids, a lack of experience in creating the right consensus around a given market approach, and, where a system like comply or explain is being used as a substitute for good old-fashioned regulation, there is a big anxiety among regulators about enforcement.

There is also in some member states concern about who is responsible for the information needed by shareholders to make the necessary judgements about the explanations. I mentioned earlier that transparency was a key element in making a code-based comply-or-explain regime effective. In the UK this means that listed companies have to produce a statement setting out whether they comply with the Combined Code and, if not, why not. This statement is monitored with a very light touch by the Financial Services Authority. Although the FSA checks to see whether the statement is there, it does not check the veracity. Nobody seems concerned about this and the culture in the UK appears to be, happily, that companies and boards do not lie in their annual reports. In other European markets the tradition is somewhat different and the regulators would be worried to delegate responsibilities in this way. What if, for example, information provided by companies on directors' remuneration turned out to be incomplete or misleading? Who would take responsibility for allowing that to happen? Would the regulators be blamed for negligence? Should it be the job of the auditors to check the governance statement? Should regulators validate the acceptance or otherwise by shareholders of the explanations offered by companies?

You could easily start to draw the conclusion from all of this that the idea of comply or explain simply will not work outside the UK, but I definitely don't want to leave you with such a pessimistic impression. We have to be realistic in accepting that we cannot simply roll out the UK model across the rest of Europe. But we must also consider what are the alternatives. There are, in my mind, two over-arching imperatives behind the consideration of all this. The first is that, within Europe, there is a generally shared desire to raise the standards of corporate governance as part of the effort to restore confidence in the wake of the corporate scandals associated with the end of the market boom. The second is that we do need some degree of harmonisation if we are to achieve a single capital market in Europe that will be capable of efficient capital allocation. One of the greatest advantages of comply or explain is that most European countries do now have codes and the evidence is that these codes are themselves promoting convergence in standards. By promoting codes and comply or explain we can harness this trend towards convergence and allow the market to help us create a single capital market. The alternative is to impose it from on high, for the Commission to bring forth European standards and regulations which are supposed to fit every circumstance. Just as we have found that the wide variety of different background circumstances makes the adoption of comply-or-explain very difficult to promote across Europe, so the task for Europe in creating a single body of detailed regulation is extremely hard. One firm conclusion we have reached in the Forum, by the way, is that we do not see a need for a single European code of governance.

I am now moving towards conclusions, and it is at this point that I should reaffirm my earlier qualification that you should treat these remarks as strictly personal. The points I am about to make are tentative ones and do not represent the considered views of the Forum. They should be seen simply as pointers which I believe can help map the way forward.

The first conclusion is that, notwithstanding the real difficulties, we should try to maximise the use of codes and comply or explain as a means of limiting recourse to prescriptive regulation and of promoting convergence in the European corporate governance culture. This is definitely preferable to the imposition of cumbersome regulation that cannot easily fit a variety of different circumstances.

In order to do this we need to work to develop a framework in which comply-or-explain can be made to work better. One important task is to understand where comply-or-explain can be made to work and where there is still a requirement for legislation and regulation. In the UK after all we don't leave everything to the Code. Key requirements – the obligation to have an audit and those relating to capital maintenance, for example - are rightly left to the law. On the whole, the Combined Code deals with softer qualitative areas, though these are also vital to the health of companies. What it has achieved over the years is a continuous process of evolution towards higher standards. This is in contrast to regulation, which requires an immediate change of behaviour, when it is imposed.

A useful principle that Europe could adopt is to consider each time a measure is planned is whether the objective could be achieved through codes or whether there really is a need for regulation. The Commission has, in my view rightly, done this in its current company law initiative when it suggested that companies should be obliged to provide a description of their internal controls rather than adopt the US approach of requiring certification that they are effective.

This leads on to another imperative. We will need to do some more work to understand the interconnection between the law and codes. Mostly the role of the law in a comply-or-explain regime is related to the provision of transparency. If companies are to be properly accountable to their shareholders, then they must disclose enough to those holders to make the accountability effective. Regulation therefore needs to be tilted towards disclosure rather than prescription about specific behaviour. And there is also a need to look at verification. In passing, I think it is worth mentioning that, as investors, members of the Association of British Insurers generally prefer the idea of a light touch on verification and assurance if this leads to companies feeling more comfortable about meaningful disclosures.

We also have to recognise that we will not have a uniform approach to all of this for many years to come. The background circumstances are such that there are bound to be sometimes quite sharp differences between member states in the way codes operate. On the basis that we are, however, working towards some sort of convergence we should be prepared to tolerate these differences for the present.

But the greatest pre-requisite for a system of comply-or-explain to work is the establishment and maintenance of shareholder rights. Investors generally have welcomed the initiative by the Commission, which we understand will shortly crystallise into a draft Directive, to facilitate cross border voting by investors in the EU. But there are two additional points on which we have to be clear.

One is that the right of shareholders to appoint and dismiss directors needs to be confirmed at EU level. The other is that we need to whittle down the myriad restrictions on voting which combine to give undue enduring protection to management and prevent their being accountable. Recent statements by Commissioner McCreevy on the subject of one-share-one-vote are undoubtedly very controversial in many parts of Europe, but they are certainly helpful in focusing attention on this question of accountability.

So where does this leave us? I would say that it should be clear that a code-based comply or explain approach would help Europe avoid the burden of excessive prescriptive regulation and help the market evolve towards convergence. This will require quite a lot of work in developing our understanding of what types of issue can be dealt with through codes and what will still require regulation and also of the role of legislation and regulation in guaranteeing transparency rather than imposing prescription on behaviour. It will also be necessary to accept that comply or explain will work differently in different markets for some time to come. And finally it is necessary to ensure that shareholders do have the rights they need to make the accountability chain work.

The last of these points is probably the most controversial conclusion of all, but, in putting it forward today I would also like to come back to the point I made earlier about the concentration of ownership in certain European markets. We should not presume that the sort of ownership concentration indicated by my earlier slide will endure for ever. The role of institutions is likely to grow, not least because of the need for Europe to develop funded pensions. The challenge is to find a way of harnessing this trend and using it to help develop a market-friendly approach to corporate governance which will help companies and shareholders generate value for the economy as a whole. If the Forum can help with this work, then I personally believe it will have served a useful purpose.

Questions and Comments from the floor:

Nicholas Beale, Sciteb: Peter, I wonder if you are being a little too pessimistic about how comply and explain regimes might work in jurisdictions that don't have the same shareholder rights as in the UK. I'm sure you have correctly identified some of the factors that make it work very well and I can see in theory, for example, how an inability of shareholders to vote out the board might make it harder to work in some jurisdictions. On the other hand, in practice I can't think off hand of a time when shareholders have had to resort to that option to do the comply or explain bit and of course some other continental countries tend to have a more consensual approach. So it might be one of these situations where a Comply or Explain regime might not work well in theory but might work in practice. And of course, one of the advantages of codes is that you can try a code and then review it and, if for some reason the code is fine but there is poor compliance, you can deal with that on an incremental basis. Isn't there a danger that the best will be the enemy of the good.

Peter Montagnon: I don't want to give that impression or to be that pessimistic. The fact that shareholders do have the right to dismiss boards even though it is very rarely used, is a tremendous incentive to engagement and addressing these issues. One of the problems of talking to people about the application of comply or explain in jurisdictions where shareholders are not strong is that the regulators become nervous about leaving important issues to a system where they can't see the enforcement.

Ana Llopis, Jose Felix Llopis Foundation: With respect to the ownership structure, you are also pessimistic about countries like France, Germany and Spain. Maybe in Germany, you might be right, because there are very large private companies. But in the other countries, the minority shareholders would be around 50%, not much lower than in the UK. So we are trying, and I hope the draft that comes out from the committee that is working on this in Spain by consensus is accepted when we do the consultation.

Peter Montagnon: It is simply a fact that it is very much easier to make it work when you have a large chunk of the market owned by a diversified of portfolio investors. It becomes very much harder when you have block shareholders because those shareholders are not independent and it not possible for the company to be accountable to them in the same way.

Stanislaw Soltysinski, Soltysinski Kawecki & Szlezak: How frequently have UK shareholders voted down or dismissed a member of the management board in a listed company since the time of the introduction of your code. Do they really use this legal method of mass destruction?

Peter Montagnon: The point is not that you have to use it in a public confrontation, but that because everyone knows that it is there, it prompts companies to think quite carefully about who they put forward to sit on the boards and also to engage with shareholders in a more meaningful way when there is a problem.

Ross Goobey, Hermes Focus Asset Management: I can give you a concrete example of company that Hermes was invested in. With other companies we were very dissatisfied with the board and we put up an alternative slate and got rid of the whole board and put in a new board. This was about 1998. We've had a code since 1993, the first code being Adrian Cadbury's code. The Combined Code is more recent.

Antonio Borges: We should never forget that one of the easiest ways that shareholders have to dismiss management is to accept a takeover bid and that happens all the time.

Herman Van Der Wyck, Hermes Focus Asset Management: We have been encouraged today to look at the future. There are two elements. The first is the increasing influence of hedge funds. The other is the rising influence in the stock market of equity funds. My question is, as we have not looked in that respect at the future, how do you insert those two categories which sometimes lack transparency and can sometimes be accused of not exercising their responsibilities in the way that institutional shareholders are forced to do and how can you make them comply or explain.

William Claxton-Smith, Insight Investment: While I agree with Peter that the ultimate sanction of voting against the board is important I feel that soft powers are also important. One of the main reasons that the code works in the UK is not because of the absolute powers but because of the consensual way in which the code was drawn up and most countries are now coming round to the view that either complying or explaining is the right thing to do.

Alan Macdougall, PIRC: Comply and explain for a lot of companies is an opportunity to neither explain or comply because no one is monitoring that compliance systematically. The Dutch market has recently set up a committee to review compliance with its code and in discussing any other European markets managing codes for the future, I certainly recommend they set up a monitoring committee on the code.

The second thing is that comply or explain is part of a process and in our view it is the principle reason why the US corporate crises that we saw at the turn of the century did not happen in the same way in the UK. Equitable Life, by the way was not a public company, although people continue to quote it as an example of a disaster in the UK disproving the value of codes, but it doesn't apply.

Finally it is important to establish the basis on which shareholders will act and one of the difficulties we still have in the UK is that discussion among shareholders is still happening in too narrow groupings. We need much more transparency about shareholder action to dispel the notion of groups of politically motivated men and women in dark corners plotting against companies.

Martin Wright, UK Shareholders Association: I can give examples of cases where we have taken action against a company and where we have managed to persuade venture capital trusts, which by definition don't have institutional investors to change procedures or merge. So we have used our powers in certain circumstances.

Amanda Young, CCLA: I think the merger between Granada and Carlton TV and ITV and Michael Green is another example of where UK Shareholders certainly affected the make up of a board.

Peter Montagnon: I will try to address some of the main points raised. First, the question of private equity. This is a difficult but very important issue. If you look at the world from the perspective of insurance companies and big institutions, we are obliged to invest in listed equities because of the liquidity and a lot of the discussion we are having about governance and codes is about the governance and the determination of the relationship between those companies and their institutional shareholders. The relationship between the shareholder and private equity and the firm is different because that person is always an insider. We are always an outsider and therefore you have to see the two as being quite different instruments and take two different approaches. What we do need to do as institutional investors needing a listed sector is to be careful not to impose so much regulation on the listed sector that it just dwindles and dies. We need to keep it healthy.

I absolutely agree with William Claxton-Smith that soft powers and consensus is important and the success of the codes in the UK is precisely because they have been iterated and re-iterated by the participants and that there is a clear agreement at the end of the day that this is the way to behave.

Alan Macdougall raised the point about lack of monitoring. I think it is up to the shareholders to monitor what goes on and raise questions when things are not satisfactory. One of the principles which guide our members when they are engaging is that the result, if the company acts, should be made public.

Internal Controls and Risk Management: Jaap Winter, De Brouw Blackstone Westbroek

Internal Controls and Risk Management. This, for us in Europe, is a lovely subject because finally we've got it right and the Americans have got it wrong. They came out with Sarbanes-Oxley, the Section 404 certification in particular and, my God, have they made a mess of it.

Now, it seems this is a general tone in the debate that we've had throughout the day. Let's not do in Europe what the Americans have done because they've got it wrong and, I sense from the atmosphere is in this hall, you feel relatively comfortable with that feeling. And that's the moment where I start to feel uncomfortable because, if we start to feel generally, all of us together, to feel very comfortable about the approach we have taken, we're probably missing something. I'm convinced that we need a certain level of discomfort to continue to think about matters which matter and, if we all start to be comfortable because it's still very clear what's not to be done and what is to be done, I'm afraid that we may actually end up stopping thinking about these issues. And there's a lot to think about.

I offer you a few observations about what's happening in the United States after the Sarbanes-Oxley and Section 404 in particular that should make us think. Conceptually, requiring executives to tell the market that they're in control of their procedures for financial reporting is not at all revolutionary. It is something that I think many in Europe believe that management should be doing all the time. They should be in control of their financial reporting to the market. That's one of the key things that the management of a listed company should be doing. There's no mistake in Sarbanes-Oxley emphasising that. There may be some mistake in the detail but that point, as such, is not a very strange thing to do. We have implied it in European corporate law, company law and many member states by asking executives, and even non-executives, to sign up the annual accounts of their company. It happens in my country and I know it happens in many other jurisdictions. That basically implies that you vouch for the correctness of your financial statements and you can only do that if you're pretty certain of the financial reporting systems and the control systems that underline those statements. So that's not revolutionary, not at all.

Secondly, there is some evidence that it actually has been very beneficial. It has imposed a sense of urgency on many American companies to improve their internal control systems. There was no escape for them; they had to do it and many European companies listed in the US as well. Many material weaknesses have been reported. I heard Andrew Bailey of the SEC report in Brussels that 3,400 instances of material weaknesses have been reported in the United States. That's an interesting fact. It's not just small bits and pieces. It's the real stuff where apparently internal control was not good. It was reported because they had to report it. And I think that's the most interesting element of this whole exercise – every executive of listed companies that you talk to about this will admit that going through the process of Sarbanes-Oxley and certifications has proven to be very beneficial to the company. Obviously they will complain about the detail and the cost. But they learned a lot about their companies that they didn't really know before and that was something beneficial and good.

Now obviously and rightly, I think, there are reasons to complain about the detail, about the cost of the system which are not just once off but probably will be regular costs. Some of this may be a feature of the American style of regulating, the detailed rule based style of regulating which most of us here in Europe will feel is not our way of doing things. It is also due to what is typical in the area of regulation, the first move of disadvantage; the one who regulates first is bound to be making mistakes and probably the US has made mistakes in this area as well by the overlaying detail and the extreme cost involved. And I grant that that's not the way forward. But let's not forget about the benefits that many have got out of this. The good thing for Europe is things move slowly so we have time to think. So far in Europe we're only thinking about a proposal that requires listed companies to describe their internal control and risk management systems. That's part of the amendment of the Fourth and Seventh Directives. And maybe, for now, that makes sense for Europe.

Many member states individually have taken actions already and we have to learn from these experiences. We have in the United Kingdom the Turnbull Guidance, the review of how it works and an amended version of the Turnbull Guidance on Internal Control. There's legislation in France. There's a Dutch corporate governance code which is very far reaching, but not binding. Sweden has just introduced a code and very specific guidance. We should learn from all of that and there's a lot to learn from the evidence. But we should not forget to learn also from Sarbanes-Oxley. We have to be honest and recognise where it works and where it doesn't. In the Forum we've discussed this briefly and so far we agree with the approach in the European Union that no more should be done than requiring just a description of the internal control and risk management systems. To me, that's the starting point of our thinking, not the end. I hope it will be for the rest of the Forum as well.

We should be thinking about key questions and I mention four areas of questions.

First of all, requirements to make a statement on your assessment of the effectiveness of control systems, perhaps requiring a formal certification as is included in the Dutch corporate governance code. What is the added value of such a statement? Will executives only take their internal control responsibilities seriously if they have to tell the market that they're in control and to what extent they have seen material weaknesses? Or can we rely on them to take this seriously anyway, even without having to make that statement? If we want some sort of statement, what is it actually that we want them to tell us? Is it a reasonable assurance of effectiveness? What does that mean? Do we know what that means? We don't know exactly, probably. What is the legal effect of such a statement? Many believe, and I think that's probably right, if your statement is wrong you might be misleading the market. The question is: when do we know that the statement was wrong. Or was the statement right but we added some meaning to it that actually was never implied in the statement? These are questions that we have to think carefully about before we impose a requirement to certify the effectiveness.

The second type of question: what types of risks to we want to be involved in the areas where we think the boards should look at internal control and risk management systems? Apart from internal control, the good thing about Sarbanes-Oxley is that it is only about audit and it's not really about corporate governance. It's only about the risks and the internal control systems over financial reporting. If you look at Turnbull and the Dutch code the scope is much wider and you have also compliance risks and operational and strategic risks. And under the Dutch code the management also has to certify that this whole big picture of internal control and risk management is run adequately and effectively by the board of that company, which is indeed far-reaching.

One of the key questions here is: does this distinction really matter because if any risk turns out to be material, whether it's in compliance, in operations or strategy, it will have an effect on the financial reporting. And what we've seen under Sarbanes-Oxley is that not only the strictly financial reporting processes have been assessed by the company itself and by the external auditors, but in fact the whole business. Because, if there is a material weakness somewhere in your business processes, which as such have nothing to do with financial reporting, they may lead to a mistake in your financial reporting which you'll have to then explain afterwards as a mistake that wasn't picked up along the road. And you'll have to find that out as a material weakness in your systems over financial reporting. So does the distinction really matter from this perspective? The question on operational and strategic risks: obviously there are too many risks to think of and to be able to describe for yourself and to assess carefully. And what is it that you are saying when you say that you've done that adequately and effectively? That's a very vague and confusing area and I can see why you would at least want to be very careful before requiring any assessment in those areas.

The third area of questions is the involvement of the external auditor, which is required under Sarbanes-Oxley and is not required in the Dutch code. It may be a requirement in some instances in some other European jurisdictions. Again, the question here is: what is the added value? And if you think of it, the external auditor is the fourth test that we apply in internal control. The internal control system is always the first test. It's a test of the business processes and what risks are coming out of that and what is managed and what is not managed, what is left open. Then management has to step in to test the internal control test and assess its effectiveness. And then the audit committee comes and it will have to review and test again management tests of the internal control tests. And then the external auditor comes to test whether the audit committee has sufficiently tested whether the management has sufficiently tested the internal control systems which has sufficiently tested the real business processes. What is the added value of the fourth layer of testing? We know there's a huge cost involved and that's not only the fee of the auditor; but it's also all the costs that we have to make internally within the company in order to allow the auditor to do his work because he can only do his work if you write down what your systems are. You have to document your systems. If you don't do that, the internal auditor can't do anything and that's where probably the real cost is. But what is the added value of involving the external auditor and certifying the statement that management has made itself?

The fourth group of questions: how do we regulate for this? Apart from the substance of the rules what is the best form to deal with it? Is it Sarbanes-Oxley type of hard law prescriptive, detailed, mandatory, no escape, you'll have to do it like this? Or is it the UK approach, the soft law. What works and what doesn't work? And here we have to be very careful because I don't think that what works in one jurisdiction necessarily works in another and Peter has already said it. Maybe for cowboys putting up high fences is the right thing to do. Now, to be honest, this is our experience in conferences as well. We call the Americans cowboys and they need this type of rule in order to behave. Let's be honest: Americans call us Europeans wimps. We're softies. And let's be honest about what that does to us. We're not running as fast as the Americans are. We may not need all those high fences when we're softy, touchy, feely in a nice way, but do we really perform?

And that's the ultimate question of corporate governance as well. I don't suggest that we should put high fences over a softy bunch of Europeans because nothing will come out of it. But let's think carefully about what works and what doesn't work. Barbara Thomas said something interesting in the breakout session this morning. She said comply and explain work in the UK because of the concept of clubability. I actually think you confirmed it just now by saying we don't have to enforce, we don't have to vote down. The mere fact that they know that you could do this and you're out of the club will mean that they will not do it. They will adapt to make sure they stay inside the club. Now this may work well in the UK, but I'm pretty sure it doesn't work in the Netherlands, for example. The only thing that works in the Netherlands is to be very specific about the behaviour that we want companies to perform to, whether through soft law or hard law, it doesn't really matter what type of law it is as long as you are very specific. If you don't specify what it means to have a full internal control system you don't get a good internal control system. And if you think of the Netherlands as the only country in the world which has specific legislation on euthanasia, abortion and the use of cannabis, this is all in the same area. You have to be specific, at least in the details of the regulation. You have to be specific otherwise the Dutch will not do it.

One of the biggest complaints about the very far-reaching statement that was required under the Dutch code is not so much that it is so far-reaching that you don't know what you're saying; it's that I don't have any guidance. How do I do this? Give me specific rules on the basis of which I can make that sort of assessment. Without the substance of the rules and the details of all of that I simply can't make the assessment.

These are all questions that we should look into and, again, I'm concerned that we're waiving a big chunk of these questions already because we think we don't like the answers. And that's wrong. Let's be honest and look at this from a fair perspective. Raise questions that we don't like because we're afraid of the answers. That's what we're supposed to do and I hope that's what the Forum will do as well.

Questions and Comments from the Floor

Paul Boyle, Financial Reporting Council, UK: I would like to respond to Jaap's comment that it's important to have a level of discomfort. And I think you've provided it for us this afternoon because if the suggestion is that we should introduce something like the Sarbanes-Oxley requirements, then that would make me very uncomfortable indeed.

We entirely agree with the sentiments and the ambitions of Sarbanes-Oxley to provide people with comfort that when you read the financial statements there's some reasonable prospect they might be about right. But we're not convinced that it would be appropriate in the UK and we've had an extensive consultation involving both companies and investors.

That's partly because we think that 80% of the benefits that Sarbanes-Oxley has delivered could be achieved for 20% of the costs. And partly because we're not at all convinced that the most serious errors in financial statements arise from weaknesses in internal controls rather than from other factors which would never be picked up by the internal control system. But also because, when you look at the set of risks to which shareholders are exposed and which boards of directors properly have responsibility to guard against, we're just not sure where, in the hierarchy of risks, you would place risks over the financial reporting process. There are probably other risks that management should be focusing their attention on and the great distraction of a mandatory, statutory, externally audited system for reviewing internal controls is that it is possibly a distraction from some of the real issues. So if you wanted us to be uncomfortable, congratulations, you've succeeded.

Jaap Winter: I'm not suggesting that we should have Sarbanes-Oxley regulation, not at all. What I'm concerned about is that many people are so clear in their not liking what has happened as a result of Sarbanes-Oxley that we're not even debating it. And maybe 80% of the benefits could be achieved with much lower costs. But let's find out whether that's true or not, that's what I would like to do.

Peter Montagnon: Criminal sanctions are part of the problem as well.

Jaap Winter: Which I haven't mentioned. I'm not talking about enforcement and criminal sanctions at all. Another striking thing that I've been finding out about over the last few years is that the two countries with the most prominent views of criminal sanctions in these areas are the United States and France. They have so many things in common that they're not aware of!

Stephan Howaldt, Hermes: For shareholders, corporate governance is a very international issue because we invest across borders and we go to different places all at the same time. For a company it's a domestic issue and it's an issue of domestic economy, domestic labour. So it's about the balance of power between the local and the international element. Now, it's a logical conclusion that as international investors we look to the EU with some hope that it will resolve those issues that are of an international nature. And my question is really to the panel: whether it thinks that the EU will do something about the protectionism that it seems can be exercised without sanction in many places. I think, for example, of the Anton Bennet saga in Italy and the Popolari Banks on the Stock Exchange, multiple voting rights, preference shares in Germany and also, to some extent, double voting rights in France. Or is it actually true that political reality has moved on and the free movement of capital and corporate control is maybe no longer desired and will certainly not be enforceable?

Herman Van der Wyck, Hermes: You haven't touched, Jaap, on two aspects. Enforcement and ultimate sanctions, including, in some cases, criminal sanctions. I think it is very important to focus on that for a minute for two reasons. First of all, because obviously if you have corporate governance rules you have regulations, you have codes and ultimate sanctions, particularly for fraud or deception or other serious cases, and your corporate credibility not only suffers but the credibility of the whole capitalist system is called into questions. We have had certain examples in the UK, in particular, but also elsewhere of court cases, eg the BCCI case, the Railtrack affair, which drag on for up to ten years. I think this is totally destructive for any confidence by the man in the street in what can be achieved if you have final recourse within the law. This has to be done within a much tighter timeframe, I feel, to maintain the credibility of the whole system from the beginning to the end.

Jaap Winter: I think I agree with that although it is probably true to say that applying sanctions against fraudulent behaviour vi criminal law should not be a speedy process. Criminal law is something very serious, too serious to justify running to a system where you strip away all the careful defences and protections that defendants have in criminal law just to make the market feel more comfortable. That doesn't mean to say there's nothing else that you can do. In the high level group work one of the things that we suggested for this type of behaviour, particularly, was to have at least a readily available sanction of barring directors from the office of directorship or officership, not just in the one jurisdiction but throughout the European Union. Mr Lehne mentioned it again this morning as something we should look into. That may be a way of at least making clear to the market that people who are involved in this are no longer directors of this type of company and that type of sanction is relatively straightforward, although very painful for the persons involved, but relatively straightforward and you could apply it much more speedily. That might help.

Professor Stella Fearnley, Portsmouth Business School: One of the things that has concerned me over time, looking at what happened in the US and the Enron affair, is in fact if we think about it, what it did was to create a market for lemmings amongst regulators. Because as soon as there was a failure in the US all the other regulators started to almost build on what had happened in the US and the Sarbanes-Oxley Act is, in fact, a US solution to a US problem. But the result of it has been to empower regulators in Europe, particularly, to copy the Sarbanes-Oxley act which has yet to prove itself completely.

We're aware that onthe internal control issue Section 404 has delivered some results but it's delivered results at a very high price and yet we're seeing things coming out of Europe which are copying perhaps one of the least well thought out pieces of legislation that has gone through the US in a long time and which had absolutely no due process. Now, I don't really see why we are doing this because, okay, we've had scandals in Europe but will all the regulation that is coming through now stop all these scandals in Europe? I doubt it. And the thing that worries me is we're creating a whole regulatory industry on the back of something that happened in the US. And when we look at the EU with the number of countries that we have in the EU, all with different legal and cultural backgrounds, can we really do anything centrally other than set out guiding principles and let the countries work it out how they want to work it out. Because what obviously works in Holland is not going to work in the UK and if we look at every country in Europe we're seeing the same thing. And yet we're seeing central control which simply cannot deliver because it won't work within the culture of the individual countries.

Jaap Winter: I'm not sure we're actually seeing so much central control over this particular issue. I grant there is a draft directive on statutory audit dealing particularly with auditors and their independence and supervision over the auditing profession, which is a big chunk of Sarbanes-Oxley and we put this in an amended version of the Eighth Company Law Directive. That is a sort of SOX lite; diet SOX. It deals with some of the subjects but it doesn't deal particularly with the internal control systems and, again, the only thing Europe is doing in this area is providing for an obligation for listed companies to disclose or to describe their systems, full stop. That's it. There is no impetus. And if you feel more uncomfortable after this session and you think Brussels is planning something then they might, I don't know. But the Forum is not planning something. But we should learn from the evidence. And that's the second advantage of Europe. We're so diverse that we have so many different ways of dealing with problems that we may actually find out that some of these have a more general applicability and could work for others as well. The US has the problem in that they have only one model. It might be right, it might be wrong, but then it's wrong for everyone. We have 25 different models and although they're not that different all the time, we may actually learn from those experiences.

Stilpon Nestor, Nestor Advisors Ltd: Jaap, you mentioned that Europe might need to think whether it should specify what internal control is and what we mean by internal control. That is an interesting observation because Sarbanes Oxley does not specify; it just says that you should apply an internationally recognised system. On the other hand, if one comes to the comply and explain environment of the UK, Turnbull is much more specific as to what it is that you want when you talk about internal control. Where do you see Europe going?

George Dallas, Standard and Poors: Given my accent and my family name I guess I would come across as being on the side of the cowboys. But I think I am more of the wimp persuasion, at least with regard to this issue. But I was at that same event in Brussels where Andrew Bailey spoke and my own anecdotal evidence, speaking with US directors, is that Sarbanes-Oxley is extremely provocative but I hear comments like, well I'm on the board of four companies and frankly, for three of them, Sarbanes-Oxley is a waste but for the one, boy, that made us do things that we really needed to do. And Andrew Bailey expressed it slightly differently in the context of a 2% solution. In other words in the tail end of the distribution of wrong doers we're trying to flag the two percenters. And that might be a bit revisionist from where Sarbanes-Oxley started out but if we take that point, I use the metal detector analogy in which if all 300 of us go through a metal detector and suffer those costs and the indignities and what have you, but we screen out one bad apple, then probably a lot of us would say that is worth it. So I guess my question to you from a policy perspective is how do you weigh the costs versus the benefits? If Sarbanes-Oxley or European solution, can catch one or two bad apples, is it worth it for the whole system to suffer these indignities?

Richard Smurdon, Wolters Kluwer Publishing: I serve on the American & Foreign Association Committee for Development of International Corporate Governance and I want to support Professor Winter with two anecdotal thoughts. One is the conversation which I had recently with the European Risk and Compliance Manager for SAP, the German based globally operating accounting software company. She said that they had found the compliance for Section 404 a truly excellent exercise for their company in sorting out their systems and making them think about them. Some very positive outcomes had resulted, particularly in terms of bottom up assessment, encouraging people at all levels to take their fair share of analysis of internal control. The second insight was at the ICT Conference earlier this year, hearing Congressman Michael Oxley being completely unrepentant about Section 404 and making the point that it had, in his view, restored confidence in the American markets. And his dismay at the watering down of the proposed auditing directive, that is the composition of the Audit Committee, which he thought was a serious mistake. As Charlie McCreevy says, why can't we trust each other's systems more. He said that in July this year in New York. And we need to be aware that Americans, as big investors in Europe, need to have a sense of confidence in what's going on over here and I would worry about this polarisation of viewpoints and I applaud Jaap Winter's courage in actually saying let's think about this.

Iain Richards, Morley Fund Management: Jaap, you made a fairly positive reference to there being benefit in Sarbanes-Oxley, focusing very specifically on financial reporting and auditing. And there was considerable discussion this morning about the importance of stewardship and accountability. One of the common perceptions of US financial reporting is that it's very prescriptive and focused on presentation of financial information. And I wondered what view you take, and what approach you'll be taking, in looking at marrying up the issues around the scope of internal controls and stewardship and accountability?

John Pierce, Quoted Companies Alliance: I'm just wondering if we're not getting a little bit too alarmist about all of this. We've got 9,000 quoted companies across Europe; I don't know how many real scandal problems we've had in the last ten years – possibly 20? I don't know if anybody's got a better estimate. But are we not over-regulating in this area? There were comments that concerned me in that we're almost looking to improve the efficiency of businesses. Well, it's not a regulator's job to consider efficiency. It's the job of the market to focus management's attention on the profitability of the business and its competitiveness. And I'm just concerned that we've got some regulatory drift going on before our very eyes here.

Jaap Winter: I think there were two questions about the level of detail and should we specify what internal control is and, if we do it, the risk is we do it in too much detail. I didn't say that Europe should do this. I said the Dutch need it. They don't get it done themselves. They may actually need Europe for them to do it and then you're all stuck with it. I think in some areas, if you look, for example, at the Turnbull Guidance and the Swedish guidance, we would all benefit from having a clearer understanding of what internal control actually means, what it is about, what the type of risks are that we should be looking into and there may be some best practices at least in these areas to do with these issues. So I think we should not be afraid to be more specific than we are now. Having just a rule in the Fourth and Seventh Directive, please describe your systems. What does it say? You tell me what the systems are and that's it. We've performed European obligations. I think for the time being I'm not bothered by having member states leading there. Through Turnbull, the Swedish code, the Dutch code and legislation – let's keep a very close watch on what actually works and what level of detail is appropriate and is helpful for the companies themselves. Two other comments were basically on the point of catching one bad apple, isn't that a price worth paying by all of us? This is the core of risk management. Do you really take steps to deal with a certain risk that may happen? Or do you decide that well, I can see that it might happen but the instance is so small and my effort to deal with it is so big continuously that I'm willing to accept the risk? This is the political bit of risk management and a judgement the politicians in European member states will have to make. One comment I would like to add, based on my clients – and obviously you understand that I only have clients which are good apples. But all of these good apple clients say they've benefited, even from the very costly system. And again I'm not suggesting – so don't go home too discomforted – everybody should pay these costs and we should please all do what the Americans have imposed. But some costs could be imposed on everyone to make sure that we're all doing it.

The Role of Shareholders:
Antonio Borges, Vice-Chairman, Goldman Sachs International
Alastair Ross-Goobey, Chairman, Hermes Focus Asset Management

Antonio Borges: The role of shareholders is of course the cornerstone of corporate governance. This is what forms our number one concern. And it should be a simple discussion. Shareholders are sovereign, period. And that should be the beginning and the end of it. In fact, in reality, it is a lot more complex than this. So at the Forum we have begun debating the issue of shareholders' rights, how to enhance them, what are the priorities, what are the most difficult issues and how can we move forward. It's an incipient debate. It's a very important one but it is also a very difficult one. And, as indicated here in this summary, this matter is very closely related to the systems of corporate governance and the systems of corporate control that are quite different across the world. I will highlight that point quickly.

In the US, in the UK and in Europe shareholders' rights means very different things. The way they are protected, the importance that each of those rights may have, is not the same and so we should put that in context. And then we should move on to the real issues that we will focus on at the Forum.

Well, several people today have made the point, which I think is generally agreed, that the standards in the US of shareholder protection are actually quite low and that the US system of corporate governance does not really require a great deal of shareholder protection. And in fact the main instance of representation of shareholders, which is the board, has a very different role from what one would expect, in particular because there isn't that clear distinction between governance and management that exists, for example, here in Britain. In fact, as we know, in the US the corporate governance system is very, very much based on the market and it's the capital market that actually exercises a great deal of scrutiny over management and therefore rewards or sanctions management. And it works quite efficiently. In fact, there was a great deal of discussion earlier today about instability and the value of stability. You might argue that if anything corporate managers in the US are in a too unstable situation. When you consider that the average tenure of CEOs is between two and three years you realise that there is very little that can be done in that time period. The market is actually quite ruthless but brutal in keeping people out when they don't perform well.

In fact the main right of shareholders – and this is a very important point – is the right to sell. And the right to sell at a decent price in a liquid efficient market that lets people in and out. People vote with their feet and that vote has enormous consequences. You might even argue that it has excessive consequences sometimes. We'll come back to this point a little later. So in fact in the US the key point about shareholders' rights is the right to be fully informed and therefore to have the information necessary to make the one decision that counts, which is to buy or to sell. Again, this is why the previous discussion was so crucial, or is so crucial in the United States, because the American scandals of corporate governance were simply cases of misleading the market or providing the wrong information to the market and therefore preventing the market from operating in its normal scrutiny of the performance of managers. And as also was mentioned more than once today, Sarbanes-Oxley is precisely about this and only this.

As Jaap was saying before it's more about the audit than about corporate governance. We want to make sure that managers report fully and faithfully to the market and that shareholders are fully informed and if that happens we're safe. There is nothing else that is needed. That is a very narrow definition of corporate governance but one that actually works. The accountability of the managers is to the market and the market is very powerful. Now there is one important change that is taking place in the US which is very commendable. There is today in every board in the United States a new culture of compliance. People are focusing very, very seriously for the first time on compliance. People are very worried about the risk of non-compliance, not just the legal risk but even the reputational risk is quite a concern. And that, I think, is a very positive development.

Now, if we go to the UK – everybody here knows the UK model extremely well – it's probably the most advanced, most sophisticated model. It's based upon this very clear distinction between governance and management, so clear that sometimes people even ask if we're not creating a divide and if that divide is not becoming a battlefield on boards. I think that risk has been exaggerated somewhat. And of course here the rights of shareholders are at the heart of good governance but we want those rights not to operate through the market but to operate through the various instances of corporate governance, of institutional corporate governance, meaning the boards, the general meetings and so forth. So all the effort in Britain has been focused on how do we make the board more effective, how do we give the board the resources, the structure, the composition that's necessary to really reflect shareholders' interests. And then how do we enhance the role of the general meeting and how do we mobilise shareholders to participate and so forth? I think this is appropriate because, in Britain, the market is not nearly as powerful as in the US and we all know of very many cases, or at least enough cases to be of concern, of situations of value destruction year after year in which nothing happens. The market is not powerful enough to enforce a change and to create a new solution.

Now the question, which I think Alastair will also talk about because I know it's one of his favourites, is this crucial role of the institutional investors in the British model. How can we through their influence deliver better governance? Can we give more power to the institutional investors? Is there a way of mobilising them for good governance? This is, again, very commendable. It's the right way. It might be actually a model for the future in Europe as well but there is a very sensitive issue of fair disclosure. It's not because you have 2%, 5% or whatever of a company that you have the right to privileged information. And therefore this does not give you the right to interact with the management in the way that other shareholders cannot. So if you want to have more influence you should be on the board. But most of institutional shareholders don't want to do that, and rightly so. That's not their role; that's not their mission. So this creates a bit of a problem which I think Alastair will debate as well.

Now, if we go to the Continent, as we know very well there's a completely different world. On the Continent I would argue that the main issue is not the lack of shareholders' rights but excessive shareholders' rights, at least on the part of certain shareholders. And that is a totally different world where the main concern of corporate governance is one of discrimination. As we know, European companies are essentially controlled by block holders, very often majority owners of these companies. In other cases if they're not majority owners they are sufficiently powerful to control the companies, even without

50% of the capital. Some of them are families; some of them are institutions; some of them are other private companies as we saw in the previous slide from Peter Montagnon. But that creates a totally different world. There is no more any difference between the shareholders and the management. The management knows very well who is the boss and the boss is, of course, the owner.

That distinction means that if ever any manager decides to neglect the interests of the controlling shareholders that neglect does not last more than a few seconds. So the issue is not the same as in the US of managers that abuse their power. The issue is more of controlling shareholders that may abuse their power.

Now, a very important issue here is that the European model has many advantages and there's plenty of research showing that it has, over the years, delivered better performance in many different cases, many different industries. It has delivered superior performance. And here we go back to the issue of stability that was discussed this morning. In fact, these controlling shareholders are more stable, they are more committed to the company, they are more supportive of the management, they are prepared to understand that if things are not going very well maybe the best option still is to stick with the current management and help them out and have a longer term vision. And that, in many cases, does deliver a better result, a better performance and so it should be an opposing view to the American so-called short-termism of immediate delivery of results.

But, on the other hand, one should also take into account that what's true for certain industries is certainly not true for other industries. And today we know that in this new economy in which we live there are many, many industries and more and more so, where the key factor in success, in good performance, is how quickly do you change and how much are you prepared to take risks. How fast do you introduce really radical innovation? And this involves a degree of risk taking which turns risk management into the most decisive factor of success. And the European model of committed long term owners is not really the best to deal with risk because it cannot diversify that risk away very easily. People are so committed to the assets they control that they will not be prepared to risk too much in that context. While in the more traditional Anglo-Saxon capital market it's much easier to mobilise investors to take risks because the market can deal with those risks very well. And that creates a degree of risk taking which is far superior and leads to much bolder strategies, much faster introduction of radical innovation and that does deliver superior performance in certain industries.

So we have to tone down when we discuss this issue about stability versus instability and the role of long term shareholders versus the more short term in and out kind of investors. We have to adapt that to what industries we are talking about and what the key success factors are in each one of them. What's valid, say, for the cement industry is certainly not valid for the high tech information technology or similar areas.

Now, the more serious problem of governance in the European model is that it is somewhat prone to abuse and the problem is that there is an enormous focus, sometimes an obsession, with control. When certain controlling shareholders exercise a great deal of power and that enables them, as I said, to deliver superior performance, that sometimes turns into an obsession which overrules everything and actually leads them to acquire control, or attempt to acquire control, at the expense of other shareholders.

First of all, we often have the concern of the private appropriation of collective value, let's say, but then there is the concern of how do I get rid or reduce the rights of other shareholders to strengthen my degree of control. So here what we have is a situation of block-holder entrenchment; it's not manager entrenchment. It's block-holder entrenchment and when companies begin operating in this manner the market understands what's going on. They will probably trade at a discount and they become more vulnerable to take over. That's precisely when these block-holders become even more entrenched and use more abusive methods to maintain their control.

This is clearly one of the key concerns about shareholder rights in the European model. It's that some shareholders exercise rights that they shouldn't. They abuse their power while others are left with very little say about what is going on. This gets more complicated if, as is often the case, the government is a block-holder and therefore it's the government that actually controls the company. Very often this leads to politicisation as we know very well through these Golden Shares and so forth. The European Commission has been very determinedly fighting Golden Shares, but this will take a long time to change.

The main concern that also arises from this is that the main shareholder does not have a return on equity requirement. This really distorts the market for corporate control and of course this creates a very serious problem for European integration.

Now, in this context, what are the issues that we should really focus on? First of all, why should this be a European issue, especially if there are so many differences? The main reason why this is a very important European issue is that, to a very large extent, what's at stake here is the single capital market. Because what happens is that with these differences in corporate governance systems and methods, and with different rights and different abuses, we actually are slowing down or creating very serious obstacles to market integration. And without a proper capital market, we're actually undermining the number one right of shareholders which is to sell. And this is the worst part of the current European system today, which is that minority investors in a company that does not treat them well do not have the ability to sell other than at a severe discount.

So a significant concern that we should have in Europe is that good corporate governance requires, or is very much helped, by a very efficient capital market that is the first support of the rights of shareholders and yet, without good corporate governance, we do not have an integrated capital market that is efficient enough to provide this kind of support. So we are in a catch 22 situation which is what makes this, in my view, a very important European issue. We need to remove the obstacles to capital market integration that are now emerging from differences in corporate governance systems and from the fact that, because of those differences, certain shareholders are able to abuse others. Now, indeed, these differences that turn corporate governance into a protectionist tool can be removed over time if we put the emphasis on shareholder rights – if, in fact, we manage to persuade shareholders to exercise their rights more fully and if, in particular, we get them to exercise their rights across Europe and not only country by country.

Therefore the two issues that we're insisting on - cross-border voting and eventually a slow, gradual move towards one share, one vote - will be, I think, the priority ones. Cross-border voting requires a set of solutions that we normally call plumbing, which in fact are very practical, very simple, but absolutely fundamental. If we do not get investors across Europe to exercise their rights because there is simply not the infrastructure necessary to make it happen, then we are undermining this market integration and efficiency. And second, if we move, even though gradually, towards one share, one vote, we will be removing many of the sources of abuse that exist today where certain shareholders, be they governments or others, actually manage to have a disproportionate share of power because they do not respect that simple principle.

Now, this is not a simple method; it's a very complex one. It has emerged over decades. People have built control over corporations after many, many years of development and investment and so forth. So it's not going to go away overnight. But if we can create a momentum in that direction then there is some hope that we might, step by step, make progress. And the most encouraging thing is that the market is now pushing in this direction. I think the most positive and reassuring development of the last few months or years is the degree to which very significant, very symbolic cross border transactions have taken place, cross border acquisitions in which investors in one country were persuaded to hold shares in companies in other countries, which of course can only be done if there is a degree of trust and confidence in the corporate governance system of these other countries that will make the difference. And what I think will happen is that these market developments will distinguish between countries in which you can trust in the corporate governance system and countries in which you cannot. And as this happens – and we can see plenty of examples – I think that we will create a momentum that will make it possible to improve standards and actually move more in the direction of shareholders' rights and, in particular, one share, one vote.

I think, for example, that one of the most helpful things that has happened in the European corporate governance scenario this last year was the scandal in Italy about the takeover of banks. The fact that the Italian Central Bank resisted and actually prevented that from happening created an outcry, such a degree of revolt, not only throughout Europe but in Italy itself. That is the most helpful thing that could have happened in creating a certain momentum to remove those old fashioned approaches. And that, I think, is a very good sign. So I think that part of our role will be in educating public opinion and creating this momentum such that we keep moving in the right direction.

But finally, let's never forget that both goals of performance and shareholder protection are important and that sometimes they are a little bit contradictory: to insist more on one of them you have to sacrifice the other one. And so when we talk about shareholders' rights, let's never push things so far that we actually sacrifice performance too much.

Alastair Ross Goobey: I'm going to talk about shareholder rights rather than the role of shareholders. We want equivalents by other means to what happens in Sarbanes-Oxley, but you heard from David Arculus this morning that he has actually managed to de-list from SEC regulation. Who can blame companies from wanting to do that because there are criminal sanctions and it is a very expensive business, and if we can find an equivalent way of meeting those sorts of internal control things without going through Sarbanes-Oxley 404, so much the better.

I remember saying a year ago at the Dutch Corporate Governance Conference in The

Hague that this represents a tremendous commercial opportunity for the EU and I think my words have been borne out. There's hardly been an international IPO in New York since then, whereas Europe is now becoming the home of international IPOs. Now this presents some risks. I accept that, because we may be getting some really duff companies here with poor governance. But I was delighted to hear what Antonio was saying, because I don't think in conferences like this there's enough emphasis on wealth creation rather than wealth protection, and that our role in corporate governance is yes to prevent the waste of our wealth, our clients' wealth, Let us not drive risk out of the boardroom, because that clearly is not in anybody's interests. It's a pretty good principle that sophisticated investors like those present in this room should be able to take responsibility for the companies in which they invest, provided they have the right information, the risks are clearly spelt out and they are reasonably confident that what they're being told is true.

That's a preamble to how do we get from where we are now to where we would like to be. We heard from Commissioner McCreevy that he's going to present his draft directive to his colleagues before the end of the year. It's reasonably clear, of course, what's going to be in it from the two consultations that the Commission has carried out on the subject of shareholders rights. And Peter Montagnon made it absolutely clear, and I couldn't agree with him more, that this is not self regulation, that it is regulation by the owners. But if the owners don't have the ability to execute their shareholder rights, then the managements really have a free hand. And it is very important that we do get minimum standards within the EU by which we, the investors, or the representatives of the owners, can execute those rights.

Those of you who have got very little to do with your time may have read all the consultation documents and all the responses. One of the things that the Commission did for the Forum was to collate all the various rules that there are in Europe for the various elements of voting shares, annual meetings, proxies, and so on, and I undertook to analyse this for the Forum and I think there are some very interesting elements to it which makes it so clear that we need to have some commonality or minimum standards at least about these issues. And this is the sort of thing that we feel makes the case for a directive.

I'll just give you some examples. Within Europe at the moment, Notice of Meetings can be between 7 and 30 days. Sometimes the Notice of Meeting only appears in the official public print rather than being sent to shareholders. We will be interested to see what number, if any, the draft directive comes to.

Record Dates against blocking. I think most people have now accepted that blocking is not the way to go, and that Record Dates are preferable. But then there's a great debate still going on about what is the appropriate date for Record Dates. In Europe at the moment they vary between 48 hours and 15 days. What is the right maximum number for shareholders to be on the record as being able to vote, but not actually own the shares?

Restrictions on proxies. There are some very bizarre restrictions on proxies. Antonio will correct me if I'm wrong but I like particularly the Portuguese restriction on proxies, where a proxy may only be granted to members of the Board of Directors, spouse, ancestors or descendants of the shareholder, or to other shareholders. In many countries, custodians can't vote their client's shares without a special proxy and explicit instructions from the ultimate investor. In Spain, the concept of custodian does not exist so there are all sorts of things that we need to iron out in the directive.

Access to the AGM Agenda varies between 0.5% in France to 20% in neighbouring Belgium. So there is a tremendous diversity in what you can do in terms of accessing the AGM Agenda, in other words, making proposals for resolutions or directives. Only a minority of the 25 states in the EU currently allow electronic voting, and we don't have a definition of who the ultimate owner is, and I think the directive is likely to remain silent on that question because it's just going to raise too many questions.

Going back to what Antonio was talking about, the cultural differences, Deutsche Borse was a very interesting experience for everybody concerned. It was a dialogue with the deaf in some ways in that the American hedge fund managers, and even some of the British hedge fund managers, didn't understand what German law was about meetings and against that the Board of Deutsche Borse was very surprised that anybody would want to vote on such a transformational transaction. And so there was really no meeting of minds on this at all.

So going back to David Jackson's question about looking forward to things that we, the shareholder representatives, the institutional investors, want to look for, going forward what is necessary in terms of shareholder rights in Europe. Well, obviously, the ability to elect or remove Boards of Directors, the ability to put shareholder resolutions and call special meetings with shareholders. And an interesting one from the point of view of the things that Hermes Focus has been doing, the ability to consult with other shareholders on concerns about individual companies without being thought to be in concert, and what is more, to be able to talk to companies on an insider basis without falling foul of regulation or other corporate codes in Europe.

When I describe what Hermes Focus often does in inviting companies to make us insiders for brief periods about specific issues, my German colleagues look at me askance and say, that would be illegal in Germany under any circumstances. I'm not sure whether that's true. I'm sure that somebody could confirm that for me. But I do think that these sorts of questions have to be ironed out and I think it would be a pity if the law in Europe constrained investors from acting together in the interests of all shareholders, rather than just one shareholder, in order to get good governance and good results and good management and good strategies and so on.

I think shareholders still want not to be diluted without their say so, so the issue of large amounts of shares, or large amounts of preference shares, without the permission of the existing shareholders should not be allowed. We should have some way in which Boards are accountable to shareholders for remuneration policies, because remuneration policies are where there is a transfer of value from shareholders to members of Boards, whether it's a management board or whether it's a unitary board. The ability to approve major transactions is, I think, very important for shareholders. The ability to approve bids when they come in and for them to be reflected to shareholders if they are bona fide bids. And going back to the question that was raised by Commissioner McCreevy earlier today, the question of one share, one vote. I was very disturbed to hear Peter Butler promoting the idea that one set of shareholders should be allowed to steal assets from another set of shareholders. I'm sure that debate will continue.

And so there are lots of things that need to be done. The directive is going to be an important step. I hope and believe that, because the consultation's been so wide, what we get won't be of any great surprise. The Corporate Governance Forum have certainly recommended that we only do what is necessary to make it possible for institutional shareholders and private shareholders to vote their shares on a cross board basis across the European Union.

Questions and Comments from the floor
Questions were taken in batches and then answered together

Christian Strenger, DWS Investment: A short comment on Antonio Borges' description of the European landscape as being one of block holders. I think that may be practically no more in most European Continental countries, Germany, for one. For example, between 40 and 60% of the large Dutch companies are now owned by institutions, mostly international ones.

Don't get misled by the Volkswagen story that has attracted so much comment. That is an exception. And Volkswagen is a thinly capitalised company anyway.

There is the opportunity for change also in Germany, but what is not happening is that the institutions that now own all these shares are expressing themselves adequately and certainly not in terms of voting. I think we should really urge the European Commission to come up, if not with a directive, at least with a very strong recommendation that institutions must vote their shares. I think that's part of their fiduciary duty anyway, but some must be helped. I'm not a firm believer in the idea that Jaap Winter more or less said, it's so nice in Europe, we have 25 different countries and so on. There must be clear cut rules on certain weighty issues and this is certainly one.

Andrew Clearfield, Investment Initiatives: I think that it's important to distinguish when discussing these various national characteristics which Antonio gave a superb summary of, that some of the biggest problems occur when you have companies which are trying to hide behind national characteristics, but in fact the company is characteristically different. You hear a great deal of talk about the good qualities of controlling shareholders and the kind of monitoring effect that they have, precisely from companies which no longer have a controlling shareholder and where in fact you have entrenched management which is trying to usurp the same privileges without have their own capital at risk that you had with block shareholders before.

In the UK we've had problems in the past. I remember the many problems we had in the clubbable environment where we had non members of the club, like the Maxwell Enterprises, which were basically offshore enterprises which were not subject to scrutiny, and like Polly Peck, where they were able to completely evade the sanctions of the club, if you will, until the situation absolutely exploded. And in the United States we have companies who love to talk about their need to maintain an entrepreneurial perspective and to reward their executives for entrepreneurship often exactly at the time when they are no longer entrepreneurial companies. So I think when we discuss these sorts of models we have to remember the normative sort of perspective that they give and that the most important problems usually come when the norms no longer apply. And this is exactly when shareholder rights and protections become the most important.

Peter Butler, Governance for Owners: Your response to paying an extra dividend to long term shareholders reminds me of when I first raised with you the issue of whether non executive directors should be rewarded in shares, which you disagreed with to start off with, and then we managed to change your mind. The issue is not about good shareholders and bad shareholders. You're not a bad shareholder if you buy today and sell tomorrow, nor is it about stealing. The issue is that being a good long term owner, taking the responsibility of being a good long term owner, is costly. You have to do a lot of things, and we're looking for market mechanisms which will help to recover that cost. And therefore the idea of some sort of small dividend to help reimburse the costs of long term ownership would help to readdress the long term/short term problems. And I look forward to having continuing debate with you.

No name given: I'm a happily retired private person and I'm Dutch and that means that my retirement is independently and fully funded, even the Government part of it. Why do I make the point, a couple of times today that this whole discussion of corporate governance shouldn't be steered or influenced too much by lawyers? Because the entire discussion on the role of shareholders seems to be a legal discussion. So I'd like to make one additional point and invite the comments of the three of you, and that is, will corporate governance in France, Italy, Spain, Germany, not change dramatically only once those countries have a fully funded pension system? Then you have shareholders, and you can discuss the role of shareholders, because if you haven't got them, then there's no need to discuss them much further.

Ian Richards, Morley: Alastair, you mentioned the importance the EU has as a sort of centre internationally for IPOs. How do you see these shareholder rights being extended to non EU companies raising capital in the EU?

Alastair Ross Goobey: Peter you were making the point that you had statistics about German core shareholders and Antonio's making the same point, and Christian is saying that, actually it's changing so quickly that your statistics are out of date.

Peter Montagnon: Well, that may be the case and it's always difficult to know exactly what's going on. I think, if I remember from the statistics, Germany showed a lesser concentration than some of the other countries on the graphs, and the figures also excluded foreign ownership, and foreign ownership has clearly gone up a lot in Germany, and that may explain something.

But I just want to come back to the point about funded pension. The hypothesis would have to be that this will change because you will get a much bigger role from institutions in the market, institutions who will then want to exercise the rights of ownership, and that you will then see the process working much better than it does when we've got block shareholders or when you've got the preponderance of very short term shareholders who are swirling about the markets at the moment. The longer term institutional shareholders, who are funding pension funds and will be there for the longer term can provide both an anchor and actually a sort of means of engagement with companies on governance, which is rather important. It does, however, presuppose that, when we have funded pensions in Europe, those pensions will be funded through the equity market. If you look at what's happening to pension funding here and the way that it is tending to shift into bonds, one has to ask oneself whether that will be the case. So the future isn't entirely clear.

Antonio Borges: I agree with Christian that the world is changing and it's changing rapidly, and indeed I think we're going to move in the direction of more institutional investors controlling companies or playing a bigger role, and then a more dispersed shareholder basis. In fact, in the United States in the 19th century and early 20th century, companies were controlled by families as well, and by significant block holders, and then over time, it got diluted in the market place so we are going in that direction.

However, this does create a problem, because the way companies were controlled until now has led to certain differences in performance and the European model of block holders has delivered better performance in many cases. If we don't recognise this, we don't understand the resistance to change that exists throughout Europe. Just like the Americans say we don't need to separate the Chairman from the CEO because we think this model delivers better performance, and we don't need that because the market is there to exercise scrutiny. Unless we understand those arguments, we will never understand why they don't want to converge to another model.

On the one hand, we have to realise that the European model has delivered better performance in many cases and that's an important concern. On the other hand, many of the control positions that exist today were built over the years with a great deal of investment at very high cost, and people don't want to be deprived of that overnight. In fact, they are prepared to sue over that one issue. So, the move towards a more equitable one share, one vote system and one in which we prevent people from exercising control and appropriating privately the collective value is going to take some time and it's going to require some grandfather clauses and it's going be probably pushed and led by the market, because the market will demand this, and those who are out of it will be paying a price for that. It's the only way in my view that we can move forward.

I also agree with the point that because certain models worked well in the past, it does not mean that they are still working well. It's at the time when the norms are changing that problems may arise, but we cannot neglect the fact that they worked well for a long time and that's why people resist change.

I have a bigger issue with the longer term or premium to longer term shareholders. I think that there's a distinction between long term shareholding and active ownership. Active ownership is when you actually exercise a degree of control. You're the owner of the company and you exercise your right as owner, and you exercise a degree of control, and therefore you have a special role in appointing the management and you have special rights to the cash flow of the company and so forth, and as everyone knows, that leads to a control premium, so you don't need any compensation. The market provides you with that kind of compensation, if necessary, and the concern we have is when that control premium becomes excessive and, in particular, when transactions mean that that control premium is appropriated by some with no sharing at all of that value with minority shareholders. So the argument that small minority institutional investors who do not have any particular control power should be paid a special dividend, for me is not really a very coherent argument. You don't need special premium for long term control shareholders. They already have it. As for the others, I think, I'd side with those that say shareholders for one day or for ten years is pretty much the same.

Now, going back to the role of short term and longer term shareholders, I think it's very important, as Christian was saying, that people vote their shares, but I think most of the problems we've had in Europe with corporate governance is precisely when people decided to vote their shares and the establishment was not happy with the way they voted. So I think we should indeed force people to vote their shares, but then we have to accept the consequences of that. Otherwise it does not make much sense.

And, finally, there is no doubt that when pensions are fully funded, we will have a different mass of capital with a long term outlook and a different strength in capital markets, and therefore a different model of corporate governance. That will help, but it's not required. And I'd like to point out, if you just look at what's happening across Europe today, if you look at the case of Spain, where there has been enormous progress over the last few years in terms of standards of corporate governance, companies have been able without any funded pensions systems to raise their standards of corporate governance, because they have been able to generate a degree of trust that was not there even ten years ago, they have been able to leverage the capital markets much, much better and they are now feared throughout Europe as the great acquirers and the great consolidators, which is something you don't see in other European countries and which I think is significant of a good model of progress in the right direction. Far from perfect, but at least progress in the right direction.

Alastair Ross Goobey: Peter, one question that Ian Richards asked, which I think you've been involved in making representations to the FSA about, is this question of whose governance are these international IPOs going to be under? The FSA is certainly looking at these IPOs from interesting companies which are based in Gibraltar or Kurdistan or wherever they're coming from, and it's great to have them in the UK, but I'm sure there's disaster there somewhere waiting to happen. That's what a vibrant market should have. But they should be under somebody's corporate governance codes. Has the ABI been involved in this?

Peter Montagnon: A number of investors have approached the FSA on this point, and I think it is actually a good question to ask, because as we are having more overseas companies come into the UK market, we obviously do need to be sure that we are preserving the quality of our market, and actually a lot of this is what we've been talking about. The existence of the codes and comply or explain and the way that companies respond to it is actually what creates quality and trust in this market. It is actually terribly difficult because when you get overseas companies coming in, they're coming from different background and they can't necessarily adopt exactly the same qualities and approaches that we adopt, and so we,ll have to think quite carefully.

I think the principle is that we need to watch the quality and that means that some of our values and basic principles have to be established here and this is an important point to bear in mind. But can I just say one other thing? I was listening to Antonio just now talking about one share, one vote and I felt it was rather a pity that Jaap has had to leave early, because he seemed to be speaking in favour of regulation and saying that the Dutch won't do this unless they're forced to. Well, it just so happens within the study that we did with Deminor, Holland came out as one country where actually the rights of the shareholders in terms of one share, one vote are particularly weak, and so that seems to me to establish a connection between having good shareholder rights and the ability to avoid intrusive regulation.

Alistair Ross Goobey: For those of you, particularly the French, who are worried about the fact that we are overstepping the working time directive because we've all been working here today for the last eight and a half hours, it's all right. Britain has an opt out, so we can go on... But I think it's time to draw the conference to a close, and I am going to ask Pierre Delsaux to come up and give us a summary of what we've heard and learnt today, and to give some feedback from the Commission.

Summing Up: Pierre Delsaux:

It's always difficult to do a conclusion after a long and rich conference like this one but clearly the number of people present today and also the quality of these people and the fact that so many of you have decided to stay until the end of the conference, demonstrates the importance of the topics and the fact that corporate governance now is a reality and will remain a reality for the future. Actually we discussed on what we should do, what should be the best practices, but nobody said we shouldn't have good corporate governance practices. I think there is a consensus that good corporate governance is good for companies, is good for investors and in general today is good for the economy as a whole.

On what we should do to try to improve corporate governance in Europe, I've heard a number of important messages and have tried to group them around a certain number of key words. First – better regulation. Second – shareholders rights. Third – last resort regulation. And finally – Wimbledon!

Better regulation. I believe there is a clear agreement that we need to regulate better, that we need as a Commission to consult widely and give a real opportunity to all stake holders to participate in the process of elaborating legislation at community level, or at least to decide what should be done at community level.

There's agreement on the principles but we still have to improve on the content of consultation. The consultation process is not necessarily perfect, some times a too short period to respond, too many consultations, too many texts to be discussed by stake holders. Also I've heard an interesting comment that when we have consultation, we should have a vision. We should explain where we want to go, just so it's easier for stake holders to be in a position to respond to the consultation process. And I believe that's an important and fair statement. We should give you a vision of what we want to do because that's important. And would help to focus your responses.

I've heard also certain comments saying that it's good for the Commission to do better regulation, but that other institutions should comply or explain when they do not comply with better regulation principles. And there was obviously the specific comment that better regulation is important also for the Parliament. If they want to make some modification to the text that is being proposed. And then they should produce an impact assessment justifying the change that may also be something on which we need to reflect at community level.

So then to shareholders rights. All speakers have mentioned at one point the word, shareholder. And that's normal because we all know that shareholders are the key of good corporate governance practices. You run a company for shareholders above all. Shareholders are fundamental for any company, so it's normal that shareholders have appropriate rights. They need to have transparent information on what's going on. They need to have voting rights. They should be in a position to vote not only on a domestic basis but also on a cross border basis. That's fundamental if you want to create an integrated market in Europe. And that's also fundamental if you want to have comply or explain principles becoming a reality in all countries of this community.

Now, as it was explained by several speakers, we have different situations. The shareholding structure is different in different countries. It's moving even in Germany, as we've just heard, but still we have more blocked shareholders in certain countries than in others. That's important with respect to shareholders rights and the way they will exercise their rights in companies.

We also have difficult issues to resolve. One share, one vote. Very sensitive. Is it good to ask for one share, one vote? I've heard dissenting views on this question. And, in any case, even if you want to move to one share, one vote, it will be a lengthy process, a difficult one, with many obstacles and many problems to be solved if we want to achieve it. And again, we have to take a decision. Do we really want to achieve this goal? It will certainly be one of the questions for the consultation exercise.

Another difficult issue concerning shareholders is the question of hedge funds. What should we do with hedge funds? You heard a very lively debate before lunch on these questions. Do we need to regulate? Which kind of regulation? Do we leave the market to decide? Are they good or not? Are they bad, hedge funds, or are they something which we should encourage? It is a very open and very sensitive issue, but also an issue on which probably we'll have to at least take some kind of position.

Finally, on the question of shareholders rights and the question of voting on a cross border basis, as you know we are going to propose a directive on this issue. It will be, I hope, a framework directive. It will probably be our Christmas gift to you. I am sure you will spend your Christmas vacation reading the text, so you will be ready to make criticism at the beginning of next year. More seriously, we can see that shareholders voting rights are fundamental, and again we don't want to regulate everything, every detail of voting rights on a cross border basis. But it's important that at least we consider that there are certain minimum principles being defined at community level, if we want to achieve a real integrated market and to be sure that shareholders can exercise their votes on a cross border basis.

And thirdly, last resort legislation. I heard the message several times that lawyers should not lead the debate on regulation. It should be left to the market and practitioners. That may be an appropriate message, that we shouldn't have legislation just for the sake of having legislation. We should have legislation which is really needed.

Another important topic, which was raised several times is what should be the balance between self regulation and regulation imposed at community level? Do we need legislation at community level? Do we need legislation may be only at national level? These are very important questions which probably will be the basis of the consultation exercise we are going to conduct on the Action Plan. What do we need to do at community level? Do we need to do recommendations? Do we need to do legislation or should we do nothing? From this point of view, again I've heard different voices. Many people have said please don't copy the Americans. Don't do a Sarbanes-Oxley in Europe. Even if there are some benefits, it's too costly and if you are in the States and you have to face Sarbanes-Oxley, you want to de-list. On the other side, I've heard the comment by Jaap Winter that we are too soft in Europe, that actually we will not achieve what we want to achieve because we need more legislation; we need to be tougher. Again, that's a very important debate on which I'm sure the consultation will cast some light.

Finally, Wimbledon? Why Wimbledon? Because I've learnt today, which is not a surprise for me, but Wimbledon is apparently the best organised tournament in the world. And I would say that this conference was very well organised. I know that apparently no British players ever win Wimbledon. But at least today, the DTI, the UK Presidency and Hermes evidently are clear winners. So congratulations to you for the hard job you have done.

This is the third conference organised by the Presidency on this question of corporate governance. I believe, and I hope, it will not be the last. I'm sure that another one will be organised in the future. As I said, it is important for us because consultation is, of course, for the Commission to ask questions, but it's also important for the Commission to support unity, to listen to all stake holders, to see your reactions, to understand what your concerns are, and also to listen to your suggestions. So from this point of view, this conference has also been very useful for us.

Thank you.