



ICGN backs EU takeover reform

ICGN chairman Peter Clapman has written to the European Commission to support the introduction of improved investor rights in European takeover contests.

In a March letter to Frits Bolkestein, the EU internal markets commissioner, Clapman wrote: "It is desirable that uniform guidelines for takeovers be established by the EU as a whole, provided that such a directive does not reflect a 'least common denominator' of the existing laws of the member states. The object of such legislation, we feel, should not only be to ensure uniformity among the members of the EU, but to encourage the best practices currently found rather than those that are questionable."

Overdue

From the perspective of the international investor, reform of takeover laws in Europe is long overdue. In most continental European markets, company management is well protected from hostile bids. Unequal share voting structures, 'loyalty' voting rights, and other voting rights restrictions mean that it is usually management and the board, rather than shareholders, that decide the outcome of control contests.

Don't miss ...

The Eighth Annual Conference of the International Corporate Governance Conference will be held at the Palazzo Mazzanotte, the Italian Stock Exchange, Milan

July 10-12th, 2002

See Page Four for details, or visit www.icgn.org

In order to facilitate a single financial market, EU institutions have long sought to bring pan-European regulation to this area and to improve investor rights. These moves have been resisted by vested interests in member states where takeover defences are most prolific, such as the Netherlands, Sweden and Germany.

After 12 years of negotiation, a European Takeover Directive looked finally to have been achieved last summer, only to fail at the final hurdle when it was defeated by a single vote in the European parliament.

Winter time

But Frits Bolkestein is determined to resurrect the core principles of the doomed directive. Last year, he charged a High Level Group of Company Law Experts with examining the core impediments to improved investor rights in Europe. The group is chaired by Jaap Winter, a legal adviser to Unilever.

Winter's committee reported in January 2002, and made far-reaching recommendations for reform, including:

- companies should disclose all defensive measures, such as unequal share voting structures, cross-holdings, etc
- takeover contests to be decided on a shareholder vote, taken on a one share, one vote basis
- acquirers amassing 75% of the shares should have the right to buy out the remaining shares, government-held 'golden shares' notwithstanding

The proposals, if implemented, would boost investor rights in Europe at a stroke. But Winter's ideas face opposition from the same vested interests that sunk the takeover directive. Only in January, for example, Germany introduced a pro-management takeover code, which would be rendered moot if

Winter's recommendations were implemented.

Opposition to Winter's recommendations have also been voiced in Sweden, Denmark and the Netherlands.

Strong support

The ICGN, representing investors accounting for some \$10 trillion in investment capital, made clear its strong support for what Bolkestein and Winter are trying to achieve.

In his March letter, Clapman wrote: "We are supportive of the [Winter] Report as a very positive development and one that should advance the cause of corporate governance in this fundamental area. Indeed, the recommendations are entirely in line with the ICGN's own principles of international best practice.

"We also endorse the [High Level] Group's two fundamental principles. First, that the ultimate decision regarding the success or failure of a bid should be left to the shareholders and the shareholders alone ... We are similarly in agreement with the second, that there should be strict proportionality between a shareholder's equitable interest in the company and his voice in exercising ultimate control over that company. This is what we mean by 'One share, one vote.'"

The letter said that Winter's views on how the mechanics of a takeover bid should work were in accordance with the ICGN's views. "When a bid has been tabled, we believe that the board of directors, which is ultimately responsible to and for the shareholders, should be obligated to submit such bid to the shareholders for their approval or rejection. Specifically, the [Winter] Group recommends that the Board be 'neutral' in mediating between existing Management and the shareholders once a bid has been launched. We think this is a good rule". (continued on p2)

One share, one vote

Unequal share voting structures are commonplace in continental Europe. A variety of devices are used, including the issue of stock with restricted voting rights, the use of voting caps, and pyramid structures.

Clapman's letter said: "The ICGN has stated in its guidelines on shareholder voting that the practice of issuing separate classes of common shares with different voting rights for each and restricting or trying to restrict the ownership of the shares with greater voting power to a particular group of shareholders serves only to curtail the right of shareholders to vote.

"A voting cap, or some sort of declining proportionality weighing upon those shareholders who possess, or acquire, a significant part of a company's equity – usually more than one to three per cent – can serve to protect a management

from outside influence without itself having to own a significant percentage of the equity."

Government protection

Following the wave of privatisations in Europe during the 1980s and 1990s, there are still numerous formerly state-owned companies protected by a government-owned 'golden share.' Clapman wrote: "Golden shares' and the like, even if well-intentioned, are still distortions of the voting power, and have the practical result of decreasing the value of other shareholders' holdings."

A widely-used device (in France in particular) rewards shareholders with improved voting rights the longer they hold the shares. But while shareholder loyalty is an important principle, the device should still be seen as an anti-

takeover device according to the ICGN: "Shareholder schemes which 'reward loyalty' with double voting rights are as suspect from this point of view as those which are blatantly hostile to the encroaching outside shareholder: both may be used to permit an entrenched inner group to retain control of a company with less of their own money than they otherwise would have needed to invest."

Finally, Peter Clapman's letter supported Jaap Winter's call for improved disclosure: "We also approve the Group's emphasis upon greater transparency of companies' capital structures. Often, the control of a company is made complicated, and kept largely confidential in ways that outside shareholders cannot fully understand. The result of this poor transparency is inevitably an underpricing of the asset."

View the full transcript of Peter Clapman's letter to Frits Bolkestein at www.icgn.org

ICGN lends weight to voting debate

The ICGN's efforts to smooth the process of cross-border share voting have been picked up by a European panel of experts.

Jaap Winter, legal adviser to Unilever and a member of the ICGN's Cross-Border Voting Best Practices Committee, was appointed by the Dutch Ministry of Justice to lead an enquiry into how voting procedures across Europe could be improved. The committee has issued a draft report, and its final recommendations will be forwarded to the EU's High Level Group of Company Law Experts, also chaired by Winter.

The High Level Group is also considering ways of improving investors' rights in takeover contests – see 'ICGN backs EU takeover reform' on the front page of this issue.

Winter will also be speaking at the ICGN's 8th annual conference in Milan, July 10-12th.

The unknown shareholder

The problems of voting shares in foreign companies in Europe are manifold. For a start, says the committee, "it is extremely complicated to ascertain who the actual shareholders are of listed companies in Europe." Companies themselves frequently don't know who holds their shares. This in turn makes providing information or ensuring that votes are being cast all but impossible.

The committee asks whether these problems should be tackled by regulation or left to market forces to solve. And, if regulation is the preferred option, should it take place at the EU level or left to member states?

The committee says that there are three main issues to be solved:

- the identification of the ultimate investor
- ensuring that these investors receive sufficient, timely information relating to voting issues
- ensuring that the investor is able to exercise their voting rights

The Winter and Wilcox committees will be keen to compare notes. Earlier this year, John Wilcox's ICGN committee carried out a survey of fund managers, custodians, and registrars to establish where the bottlenecks in the international voting process lie. Additionally, it is carrying out a detailed 'post mortem' of the voting process at six global companies.

The Cross-Border Voting Committee's survey attracted responses from 18 institutional investors from the US, the UK, Canada, the Netherlands and Switzerland, together representing \$8 trillion of investment capital. Two of the main issues they raised were tight ballot deadlines and shareblocking rules in some markets that prevent trading ahead of annual meetings.

The survey revealed that respondents are keen to vote their shares. All but two institutions replied that it was their policy to vote all shares, whether foreign or domestic. But while 13 said that they were able to fulfil this policy at home, only eight reported being able to hit their target overseas.

An effective audit trail is another missing piece. Half of those surveyed said they had no means of telling whether cast votes ever actually reach the company.

Wilcox will report on both these initiatives in detail at the ICGN members' meeting in Milan.

ICGN members with views on the cross-border voting process in Europe should comment on the Winter committee's draft report. It can be found at www.wodc.nl. Comments are due by June 3.

ADRs – the ICGN investigates

UK oil giant BP caused a storm last year by excluding a shareholder resolution filed, in part, by holders of American Depositary Receipts (ADRs). The clear implication of BP's move? That ADR holders are second class citizens compared to full shareholders.

ADR-holders' rights are uncertain in other areas, including their right to vote, and to participate in rights offerings.

This uncertainty comes at a time when ADR programmes are more popular than ever before. They allow non-US companies to tap the vast US capital markets without a full listing. For US shareholders, ADRs facilitate investment in overseas companies coupled with a measure of SEC protection. Given their increasing use, it is especially vital that the rights of ADR holders be clarified.

At its Tokyo conference in July 2001, the ICGN empowered a subcommittee to study the legal framework of ADRs.

Chaired by Jennifer Choi, of the Investment Company Institute, the subcommittee recently reported initial findings. The document is open for consultation on the ICGN website, and members will finalise the document at the 8th annual meeting in Milan in July.

ADRs are certificates issued by a US bank or trust company which represent ownership interests in shares of foreign companies that have been deposited with the bank or trust. Choi's paper outlines the principal investor rights issues

for ADR holders and suggests some remedies.

Some of the most significant concerns include:

Notice and voting materials: "ADR holders are not provided voting materials in sufficient time to be able to exercise their voting rights effectively," says Choi. Many depositary agreements include the disclaimer that there is no guarantee that ADR holders will receive proxy materials in sufficient time to vote.

Right to vote: The subcommittee says: "We understand that a standard term of the depositary agreement is that ADR holders will only have the right to vote if the issuer formally requests the depositary to ask ADR holders for their votes."

Autoproxy: Certain depositary agreements provide that if ADR holders do not vote, these shares will be assigned to the issuer's management to vote at its discretion.

Depositary Bank Must Cast Its Vote in the Same Way: In some jurisdictions, a shareholder may not "split" its vote and therefore cannot vote in favour of a proposal for some of its shares and vote against the proposal for other shares.

Shareholder Proposals: If, for example, a company only accepts proposals that are submitted by at least 100 shareholders, a depositary bank, which would be considered one shareholder regardless of the number of ADR holders the bank

represents, would not be able to submit proposals on behalf of its ADR holders.

This is what happened with BP in 2001. **Shareblocking:** The problems associated with shareblocking are exacerbated for ADR holders whose shares are blocked for even longer period of time, since their instructions must be forwarded to the depositary bank several days in advance of the blocking deadline.

The Choi subcommittee makes several recommendations for reform, focusing on short- and medium-term projects as well as longer term ones. The subcommittee notes that most of the obstacles to improved rights for ADR holders lie in the depositary arrangements, and that in the short-term the ICGN should focus on trying to improve these arrangements.

In the longer term, improvements probably rely on changing the laws in the relevant market of the issuer. For example, on shareblocking, the subcommittee simply recommends: "companies should eliminate this practice."

Download the recommendations of the ADR subcommittee at

<http://www.icgn.org/consultative/index.html>

ADR subcommittee

Jennifer Choi (chair)

David Dando

Paul Lee

Ted Rothschild

Harry Frost

Pierre-Henri Leroy

Cas Sydorowitz

Members' business

As ever, the ICGN annual meeting of members will follow directly after the annual conference. This year, that means that the meeting will start at 2.30pm on Friday July 12th at the conference venue in Milan.

The meeting is only open to members, so be sure your membership dues are up to date. If you want to pay the annual fee, or confirm your payment, please contact the ICGN secretariat by emailing icgn@icsa.org.uk

The members' meeting will include vital business, including: the revised bylaws, updates from key committees including the compensation committee's first draft of global common-denominators, and briefings by ICGN partner organisations, including the OECD, the Global Corporate Governance Forum, and International Forum for Accountancy Development.

Awards

The ICGN's Awards Committee is reviewing nominations for the ICGN's annual awards. Inaugurated in 2001, the awards are made to individuals or organisations who have markedly improved the state of corporate governance in one or more jurisdictions.

The Committee is reviewing nine nominations, submitted by members by the April 13 deadline. They come from eight countries, and candidates include both individuals and organisations. Final decisions will be made by the committee and the board, with advice from 2001 laureates.

The identity of winners will be kept confidential until the presentation on July 11, in Milan. Dr. Hasung Jang of Korea, one of last year's inaugural recipients, will present the awards.

The ICGN Awards Committee

Dr. Stephen Davis (chair)

Jon Lukomnik

Christian Strenger

Experts expected

The Eighth Annual ICGN conference in Milan will be addressed by some of the leading names in Italian business and investment, as well as by a panoply of international experts, including:

- Professor Angelo Tantazzi, Chairman, Borsa Italiana (Italy)
- Luigi Spaventa, Chairman, Consob (Italy)
- Massimo Capuano, CEO, Borsa Italiana (Italy)
- Alessandro Profumo, CEO, Unicredito Italiano (Italy)
- Alastair Ross Goobey, Chairman, Hermes Focus Asset Management (UK)
- Paolo Fresco, Chairman, FIAT (Italy)
- Sylvia van Waveren, Corporate Governance Manager, PGGM Pension Fund (Netherlands)
- Professor William Crist, President, CalPERS (US)
- Eliane Aleixo Lustosa, Investment Director, Petros (Brazil)
- James Shinn, Senior Fellow, Council on Foreign Relations (US)
- Florian Schilling, Partner, Heidrick & Struggles (Germany)
- Taiji Okusu, Managing Director and Vice Chairman, UBS Warburg (Japan)
- Domenico De Sole, CEO, Gucci (Netherlands / Italy)
- Stefano Micossi, Chairman, Assonime (Italy)
- William Lerach, Senior Partner, Milberg Weiss Bershad Hynes & Lerach (US)
- Guido Cammarano, Chairman, Assogestioni (Italy)
- Karel van Hulle, head of Unit, Financial Information and Company Law, European Commission
- Jaap Winter, Legal Advisor, Unilever (Netherlands)
- Robert Kinlock Massie, Executive Director, CERES, (US)

Companies as Citizens

8th Annual Conference - Milan
 Wednesday July 10 2002 -
 Friday July 12 2002

Plenty has happened in the world of corporate governance since ICGN delegates met in Tokyo in July 2001.

In the US, the collapse of Enron has caused Congress, the SEC, the White House, and the principal stock exchanges to suggest numerous reforms to the US governance structure.

In the UK, the government has announced high-level reviews of director effectiveness and the rigour of the financial reporting regime. In Europe, the EU has revived efforts to improve investor rights in takeover contests and when voting their shares.

Improved governance has increasingly become recognised by emerging markets as a vital element in attracting overseas capital. Earlier this year, the Institute of International Finance launched a major

initiative to support emerging market regulators in developing robust governance structures.

These developments will provide plenty of food for thought for delegates at the Milan conference. The 8th annual ICGN event marks the first time the Network has held its conference in a Mediterranean market, and it comes at a time of significant change in Italian governance.

The Italian market has traditionally been dominated by family-owned companies and by the state. But, in line with trends across Europe, many of these companies have been privatised or have been forced to open up to attract international capital.

Some of the milestones in the development of Italian governance include the publication of the Preda code of 1998, and the decision by the Italian Stock Exchange last year to start publishing companies' compliance with the Code.

8th annual conference - Key questions

Do Italian reforms in transparency and accountability go far enough to meet global market demands?

How should funded retirement systems behave as investors? Should they be as transparent and accountable as they expect companies to be?

States, companies and investors are scrambling to overhaul approaches to corporate governance all over the world. What international standards should they strive to meet?

Companies are facing unprecedented demands from investors to raise their accountability and transparency practices to world standards. But what is the real value of corporate governance - for the

economy, for investors and for the companies themselves?

How can listed companies improve their relationships with their investors?

The European Commission is wrestling with the issue of whether, and how much, to push corporate governance reform through regulation, law, stock exchange listing rules or voluntary measures. What works? What political pressures apply?

If a company commits corporate governance resources to better citizenship, can it expect better financial performance, easier access to growth capital and better relations with investors?

The International Corporate Governance Network seeks to bridge the gap between corporate management and shareholders. The ICGN is an international, informal network of institutional investors, shareholder advocates and corporate governance experts. ICGN members together hold assets totalling some US\$10 trillion.

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The ICGN Secretariat is administered by Ms Caroline Phillips, Director of the Policy Unit of the Institute of Chartered Secretaries & Administrators (ICSA).
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