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Corporate Governance

Board structures and directors' duties in 34 jurisdictions worldwide

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Contributing editors
Ira Millstein and Holly Gregory
Weil Gotshal & Manges LLP

Business development managers
Alan Lee
George Ingledew
Robyn Hetherington
Dan White

Marketing managers
Ellie Notley
Alice Hazard

Marketing assistants
William Bentley
Zosia Demkowicz

Admin assistant
Megan Friedman

Marketing manager (subscriptions)
Rachel Nurse
Subscriptions@GettingTheDealThrough.com

Assistant editor
Adam Myers

Editorial assistant
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Senior production editor
Jonathan Cowie

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Jonathan Allen

Subeditors
Davet Hyland
Caroline Rawson

Editor-in-chief
Callum Campbell

Publisher
Richard Davey

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87 Lancaster Road
London, W11 1QQ, UK
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Fax: +44 20 7229 6910

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Global Overview

Arthur Golden, Thomas Reid and Sapna Dutta

Davis Polk & Wardwell LLP

Across the globe, as the wave of post-financial crisis corporate governance reform continues, the impact of the significant burdens on the regulators that are responsible for implementing these reforms is becoming increasingly visible. At this time, we are also seeing a subtle divergence in the nature of these regulatory efforts in different parts of the world. In the United States, since the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) became law in 2010, regulatory efforts have focused primarily on its implementation, which continues to require significant time and has resulted in delays in the rulemaking schedule. In contrast, in Europe we have seen more in the way of new initiatives, including the publication of the European Commission's Green Paper on a future corporate governance framework across the European Union and the United Kingdom government's significant proposals to introduce a new model of shareholder voting on executive compensation, including a binding vote on remuneration policies.

There remain some common themes. In particular, there has been increasing focus surrounding the governance of shareholder engagement with companies. Additionally, many of the focal points in governance reforms – whether in the implementation or initiative phase – remain comparable and constant: much of the global focus continues to be on the issues of executive compensation and the quality and scope of governance disclosures, and on matters relating to board composition, including declassification, separation of CEO and chair positions, and the promotion of diversity and gender equality on company boards.

During 2012, we expect that US and European companies will experience another year of intense pressure from regulators and shareholder advocacy groups in respect of their corporate governance practices on a number of fronts. It is inevitable that the reaction to the financial crisis of 2008 and the ongoing eurozone crisis should provoke such severe and prolonged reaction. What remains to be seen, if, as and when global economic conditions stabilise, is whether these ongoing governance reforms ultimately do anything to improve the competitiveness or actual governance of individual companies of the North American or Western European economies or whether they are simply a series of responses – ranging in nature from remedy to retribution – that may be understandable, but perhaps not efficient in the long term.

United States

In the United States, for most public companies 2012 represents an opportunity to reflect on the first year of effectiveness of a limited initial number of provisions of Dodd-Frank. In particular, most companies have now lived through one 'say-on-pay' and one 'say-when-on-pay' advisory vote, and have managed to emerge from the process relatively unscathed, with approximately 87 per cent of all companies that have held their first say-on-pay vote reporting over a 70 per cent approval as of 20 April 2012. It also represents a year of new challenges, as companies face the newly effective 'private ordering' proxy access proposals as well as, for a small number of companies, the consequences of receiving a negative say-on-pay shareholder approval rate. These consequences include heightened scrutiny on the actions taken by such companies to address their compensation plans as well as the threat of shareholder derivative litigation, which as of 20 April had materialised in the form of 14 derivative lawsuits.

Aside from the shareholder advisory voting regime for executive compensation arrangements, the effectiveness of many of the other provisions of Dodd-Frank relating to executive compensation and governance arrangements has been delayed due to the significant burden of required rulemaking by the Securities and Exchange Commission (SEC). As a result, the issuance of many rules previously expected during 2011 is now postponed until 2012. If anything, given the impending November elections, there is potential for further delay in the implementation timeline, especially if there is a change in the presidency or in the balance of political party representation in the Senate or House of Representatives.

Further, on 5 April 2012, the US Jumpstart Our Business Startups Act, (the JOBS Act) was signed into law. Designed to help companies with annual gross revenues below $1 billion to access the US capital markets and promote entrepreneurship, the JOBS Act represents the most substantial legislative loosening in memory of restrictions around the US IPO process and public company reporting obligations. It significantly reduces the governance standards with which those companies must comply for a transitional period up to five years post-IPO and removes some companies altogether from the US public company reporting regime through an increase in the numerical shareholder thresholds that trigger these obligations. At this stage, it is too early to have seen the provisions of the JOBS Act play out in practice and, while it is difficult to fault the intentions behind the JOBS Act, there are already concerns that it will weaken essential investor protections and spawn a new string of painful frauds. It is at least ironic that the JOBS Act is strongly applauded by many of the same politicians who were advocates of the most 'difficult' aspects of Sarbanes Oxley. In the shorter term, the JOBS Act is likely to further constrain regulatory resources, given that some of its provisions require rulemaking by the SEC before they can become effective.

Proxy access

The most closely watched issue of the 2012 US proxy season has been the availability of the so-called 'private ordering' proxy access rules, which came into effect in September 2011 and enable shareholders of US public companies to seek to implement proxy access on a company-by-company basis by proposing amendments to companies' organisational documents permitting shareholders to include director nominees in the company's proxy statement.

The SEC's mandatory proxy access rules were vacated by the DC Court of Appeals in July 2011 and the SEC confirmed that it will not appeal that decision. Whereas the mandatory proxy access rules would have given US public company shareholders the immediate ability to include director nominees in a company's proxy statement, the changes to Rule 14a-8(i)(8) instead provide for a two-step process, available to shareholders owning at least 1 per cent or $2,000 of the company's voting securities, whichever is less, for at least one year. First, shareholders may propose changes to the company's own governing documents specifying procedures by which shareholders may include director nominees in the company's proxy materials. Second, if proxy access procedures are adopted, a shareholder may then propose director nominees pursuant to those procedures.

We have already begun to see shareholders take advantage of the new rules and, as of 20 April 2012, investors had filed over 20 proxy access proposals for 2012 annual meetings, just over half of which looked set to go to shareholder vote as of that date.

Interestingly, there have been a variety of different access standards sought in these proposals. The most common form of proposal is based on a now-revised model issued by the United States Proxy Exchange (USPX), a shareholder advocacy group. That original model requests a by-law amendment granting proxy access rights to one or more shareholders if they have continuously held 1 per cent of the company's voting stock for a two-year period, or alternatively any group of 100 holders who satisfy the $2,000 or 1 per cent/one-year requirement discussed above. The access standards sought in other forms of proxy access proposal include an ownership standard of 1 per cent for one year (Norges Bank), and an ownership standard of 2 per cent for one year (Furlong Financial).

So far, 'private ordering' has prompted change at a small number of companies. For example, February saw Hewlett-Packard become the second company to agree to submit a management resolution for proxy access to its shareholders in response to receipt of a proxy access proposal. That said, given the early stage of the 2012 proxy season, it remains unclear at this point how shareholders will vote in response to proxy access proposals and what share ownership and holding period thresholds will be favoured. It is likely that most companies will continue to wait for a better sense of shareholder support for these proposals before affirmatively taking action to implement proxy access. As it progresses, this proxy season may prove to be a fertile testing ground for whether proxy access is implemented through private ordering or whether shareholder groups will continue to pursue a federally mandated proxy access rule. Some advocates for proxy access have already stated that they intend to pursue both courses of action.

Executive compensation

New CD&A disclosure requirements in effect for 2012 proxy season

This year sees the first time that companies are required to disclose in their proxy statement compensation discussion and analysis (CD&A) whether, and if so, how, they considered the results of the most recent say-on-pay vote in determining compensation policies and decisions, and how that consideration affected their executive compensation decisions and policies.

So far, the vast majority of large accelerated filers who have filed proxy statements in the 2012 season have addressed this new requirement with disclosure that has not been surprising: companies that received lower shareholder approval ratings on say-on-pay in 2011 have provided lengthier disclosure, often addressing changes made to their compensation programmes, while those that received stronger shareholder support have simply stated that they have considered the results and decided to continue their previous compensation practices in light of the support. A small number of filers have either failed to mention the 2011 say-on-pay vote or did not discuss whether the company considered the result. As of 20 April, that omission had not negatively affected the ISS recommendations for these companies regarding this year's say-on-pay proposals or say-on-pay results in 2012, although in each case they received at or above 82 per cent shareholder support in 2011.

Say-on-pay and say-when-on-pay

For most companies 2011 was the first year for say-on-pay. Most fared well: of the 1,409 large accelerated filers that have held their first say-on-pay vote, 918 received 90 per cent approval or higher and only 127 received less than 70 per cent approval, with 28 of those failing to receive majority support. This year, companies that received a high say-on-pay approval rating at their 2011 annual meetings have generally kept their disclosure short and maintained their previous pay practices. As of 20 April, 1,025 large accelerated filers had filed proxy statements seeking a second say-on-pay vote, and of the 115 that had reported the results of these votes, only a small number (15) received negative votes, ranging from approximately 68 per cent for Qualcomm, Inc to 44 per cent for International Game Technology. All 15 received 'against' ISS recommendations.

Companies with a lower than 70 per cent say-on-pay approval vote in 2011 are inevitably facing heightened scrutiny this year, and in its 2012 policy update, ISS indicated that it will recommend votes on a case-by-case basis for compensation committee members of companies that received less than 70 per cent approval based on, among other things, the company's disclosure of its engagement efforts with major institutional investors and specific actions taken to address the issues.

At this point in the season, we can make some early observations, but it is difficult to establish clear patterns. For one, there have been examples of improvements in approval ratings since 2011: Monsanto increased its rating from approximately 66 per cent in 2011 to 86 per cent in 2012, and Jacobs Engineering Group more than doubled its rating from approximately 45 per cent to 98 per cent. At the other end of the spectrum, some companies have fared worse this year, such as Johnson Controls, who received approximately 62 per cent support last year and 58 per cent this year. However, while each of Monsanto, Jacobs and Johnson provided lengthy disclosure in their proxy statements in response to last year's votes, Monsanto did not make changes to its compensation plans, whereas both Jacobs and Johnson did. Going even further, in a reminder that a high rating in 2011 will not necessarily lead to the same result this year, there have been examples of companies that received very high ratings last year and have seen their ratings decrease dramatically; having all received negative ISS recommendations this year (mainly citing misalignments between pay and performance), Navistar International Corporation, Transdigm Group Incorporated and Concur Technologies, Inc have seen their ratings fall from approximately 99 per cent, 98 per cent and 99 per cent to 75 per cent, 54 per cent and 62 per cent, respectively.

In the 2011 say-when-on-pay votes, shareholders displayed a strong and clear preference for annual say-on-pay votes, even where the applicable company recommended biennial or triennial votes. Of the 1,395 large accelerated filers who have held their first frequency vote, the shareholders of approximately 90 per cent of those companies voted for the annual frequency. Of those accelerated filers that recommended annual frequency, the shareholders of all but one company voted for the annual frequency. Given that say-when-on-pay votes are only required to be held once every six years, we do not expect many frequency votes in the 2012 proxy season and as of 20 April, only five proxy statements had been filed seeking a say-when-on-pay vote.

Say-on-pay litigation

As of 20 April, derivative lawsuits had been filed against 14 companies who received a failed say-on-pay vote; some of these have settled, but others have proceeded to court. In an early and troubling development in September 2011, the federal district court judge in the *Cincinnati Bell* case refused to dismiss the suit and found that the advisory nature of the vote was sufficient to rebut the presumption of the business judgement rule. However, subsequent cases have reaffirmed directors' authority to determine executive compensation, with judges in Oregon and Los Angeles dismissing say-on-pay litigation suits in March 2012 and expressly rejecting the *Cincinnati Bell* finding that a negative shareholder vote alone is sufficient to rebut the protection of the business judgement rule for directors' compensation decisions. These early proceedings indicate that shareholders bringing these derivative lawsuits will face substantial hurdles even to survive a motion to dismiss.

Say-on-golden parachutes

Since 25 April 2011, companies are required to hold an advisory shareholder vote on executive severance packages (golden parachutes) in connection with M&A transactions that are presented for shareholder approval. Almost one year on, as of 20 April, 102 companies had included golden parachute disclosure and votes in their merger proxies, 80 of which had publicly disclosed the results of the golden parachute vote. All of the votes received support of a majority of shareholders, even those on which ISS had issued an 'against' recommendation, indicating that in this context, shareholders' votes are closely linked with their views regarding the overall merger transaction.

Upcoming SEC executive compensation rulemaking under Dodd-Frank

The SEC's Dodd-Frank rulemaking timetable contemplates the issuance of various rules on additional compensation provisions of Dodd Frank during the January to June 2012 time period. These include:

- proposed rules relating to clawback of compensation, requiring disclosure of incentive-based compensation that is based on publicly reported financial information and enabling the recovery of incentive-based compensation from current or former executive officers following a restatement;
- proposed rules relating to disclosure of pay for performance, pay ratios and hedging by employees and directors;
- adoption of final rules requiring national securities exchanges and associations to adopt listing standards regarding compensation committee independence and to consider the independence of those committees' advisers;
- adoption of final rules on disclosure of compensation consultant conflicts of interest, which would amend the existing rules to require disclosure about whether a company's compensation committee has retained or obtained the advice of a compensation consultant, whether the work of that consultant has raised any conflict of interest and, if so, the nature of the conflict and how it is being addressed; and
- final rules regarding executive compensation structure and arrangements for financial institutions (the proposed rules for which were jointly issued by the SEC and six other federal agencies in April 2011 and would, among other things, require reporting of incentive-based compensation to regulators and prohibit incentive-based compensation arrangements that are excessive or that could lead to material financial loss to the institution).

Governance implications of the JOBS Act

The JOBS Act was signed into law by the president on 5 April 2012. Among other things, the Act significantly relaxes the rules relating to IPOs by emerging growth companies (EGCs) (companies with gross annual revenues of less than $1 billion), for a transitional period post-IPO of up to five years. Its provisions include a significant reduction in the corporate governance standards applicable to EGCs during the transitional period, including reducing many of the executive compensation disclosure requirements that would otherwise apply and removing some companies altogether from the US public company reporting regime, through an increase in the numerical thresholds that trigger these obligations.

The JOBS Act exempts EGCs for the applicable post-IPO transitional period from Dodd-Frank's requirements to hold shareholder advisory votes on executive compensation, including say-on-pay, say-when-on-pay and say-on-golden parachute voting requirements, and executive compensation provisions requiring the pay for performance and pay ratio disclosure. The exemption also includes eliminating the detailed narrative executive compensation disclosure requirements applicable under the US Exchange Act rules; instead, EGCs will need to provide only the scaled disclosure that smaller reporting companies (generally, those with a lower than $75 million public equity float) are required to provide which, notably, do not require a CD&A section. Additionally, companies are permitted to provide executive compensation information for fewer executive officers and may present two (rather than three) years of compensation data.

For the same transitional period, EGCs are also exempt under the Act from compliance with Sarbanes-Oxley 404(b), which requires companies to provide an auditor attestation report on their internal controls over financial reporting.

Further, the Act increases the numerical shareholder threshold that triggers US public company reporting obligations under the US Exchange Act. Under the Act, the threshold would be triggered by a class of equity securities held of record by either 2,000 shareholders or 500 shareholders who are not accredited investors. This means that, overall, companies with a substantial shareholder base will be able to delay becoming subject to the SEC's public company reporting obligations generally, including the applicable corporate governance standards, until those higher thresholds are met.

Other governance topics

The topics of board declassification and independent board chairman have both attracted greater investor interest this year, and a significant number of proposals have been submitted on both issues. Board declassification proposals gained strong support in 2011 (these proposals received one of the highest average approval rates) and that has continued to be the case at early meetings this season, with these proposals receiving approximately 77 per cent approval at Emerson Electric and 85 per cent approval at Johnson Controls. Approval of independent board chair proposals remains relatively rare among large-cap US public companies, and in 2011, received majority shareholder approval at only four companies.

With 2012 being a presidential election year – and the first one after the Supreme Court's *Citizens United* decision – we expect to see greater numbers of shareholder proposals seeking disclosure of political contributions. As of 20 April, 65 shareholder proposals on this issue had been brought during 2012. ISS changed its voting policy for 2012 for shareholder proposals seeking disclosure of political contributions and will now generally vote for these proposals rather than on a case-by-case basis.

Finally, exclusive forum provisions in charters and bylaws, under which derivative suits and other shareholder litigation must be brought in the courts of the company's state of incorporation, drew some attention during the 2011 proxy season, and momentum behind these provisions continues to gather pace, but slowly. These provisions have now been adopted in some form by over 200 companies, and we have already begun to see the emergence in 2012 of shareholder proposals seeking to repeal them. In the midst of continuing questions as to the enforceability of such provisions and the level of shareholder acceptance, no consensus on this topic has yet emerged among institutional investors, and the 2011 votes were close and had mixed results.

Europe

Key governance themes across Europe over the past 12 months have included the continuing difficulties in achieving diversity and gender equality on company boards; ensuring the quality of European companies' corporate governance disclosure, with a focus on the effectiveness of the 'comply or explain' principle and the quality of 'explanations' thereunder; and issues relating to companies' executive remuneration policies, stewardship and investor engagement. All of these topics were identified in the European Commission's 'Corporate Governance Framework' Green Paper (the Green Paper), which was published on 5 April 2011, as potentially in need of focused improvement – including, possibly, by implementing a more uniform governance regime on some topics at European Union level. The feedback from the public consultation on the Green Paper was published on 15 November 2011, although as of yet the European Commission (the Commission) has not announced resulting policy or legislative initiatives.

The Commission also raised in its Green Paper a general question – but one important to the way in which governance operates in the EU – as to whether different corporate governance regimes should apply in the EU based on the size of listed companies. The majority of respondents were not in favour of this, and particular opposition came from businesses and investors, principally based on the flexibility already provided to companies of all sizes by the 'comply or explain' principle; the benefits that a single, EU-wide governance standard provides from an investor comparability perspective; and the difficulties in establishing meaningful size criteria across the EU. Respondents were similarly opposed, generally, to the Commission's proposal to extend the application of corporate governance requirements at EU level to unlisted companies.

Director remuneration

In the UK, in January 2012 the government announced a package of measures that would make significant changes to the executive remuneration framework, both in terms of governance and disclosure. Historically, the UK has been something of a front runner in the say-on-pay regime, as an advisory say-on-pay vote on companies' director remuneration reports included in their year-end annual reports is already in place. However, following its January announcement, the government launched a consultation on a proposed new model for shareholder voting, which would apply to the remuneration of directors in UK incorporated quoted companies and includes:

- a new annual binding shareholder vote on future remuneration policy, with an approval requirement of, potentially, up to 75 per cent;
- a new binding vote on exit payments over one year's salary; and
- an annual advisory vote on how remuneration policy has been implemented in the previous year, with associated requirements to disclose how the results of the vote have been taken into account.

Under the new proposals, companies would have to set out, at the start of the year, a proposed pay policy for the year ahead, which would be put to a shareholder vote. Companies would be required to act within the scope of the remuneration policy agreed by shareholders and, if the binding vote is lost, companies would have to fall back on the last policy to be approved or hold a further shareholder vote on revised proposals. In addition to the binding nature of this vote, the increase in approval threshold has also raised concern on the basis that it could give excessive power to minority shareholders. At this stage, the government has not proposed to implement a frequency vote, instead suggesting that the binding vote on remuneration be held annually.

The government will confirm the exact measures it proposes to take later in the year and expects, subject to parliamentary process, to bring legislation on new shareholder voting rights and revised reporting requirements on director remuneration into effect in spring 2013.

Reflecting the more widespread focus on this issue, the Green Paper also solicited feedback on whether disclosure of companies' remuneration policy, the annual remuneration report and individual remuneration of executive and non-executive directors should be made mandatory at an EU level, and whether the remuneration policy and report should be put to a mandatory shareholder vote. Respondents demonstrated support for both of these proposals introduced, although notably most in favour of a shareholder vote indicated that the vote should be advisory only. Almost three-quarters of respondents were in favour of disclosure of individual director remuneration (which is not currently the case in all EU member states), although some who were not in favour thought that this would interfere with the privacy of the concerned board members and could have the effect of driving remuneration levels upwards.

Diversity and gender equality on company boards

The question of how to increase diversity in the boardroom, particularly with respect to gender equality, continues to be hotly debated in Europe. Last year, the Commission asked listed companies to adhere to a voluntary pledge to increase the percentage of female directors; if taken, the pledge requires that any signatory company reaches a target of 30 per cent female board members by 2015 and 40 per cent by 2020. On 5 March 2012, however, the European Commission published a report indicating that only 24 companies had signed up as of that date and that, more generally, only limited progress has been made in increasing the number of women on boards. Pursuant to these developments and in light of the widespread rejection by the majority of Green Paper respondents of the notion of mandatory quotas for women on boards, the European Commission launched a public consultation in March this year to identify appropriate measures for addressing what it sees as the persistent lack of gender diversity in boardrooms of listed companies in Europe.

In the UK, since the publication of Lord Davies' report on gender diversity in the boardroom in February 2011, various consultations have been held regarding its recommendations and the majority of those recommendations are now in various stages of active implementation. In particular, following a consultation held last year, the Financial Reporting Council (FRC) announced in October 2011 that it will be amending the UK Corporate Governance Code (the Code) to require listed companies to publish their policy on gender diversity in the boardroom and report against it annually and to consider diversity as a factor when evaluating the effectiveness of the board. The UK government's department for business has also conducted a consultation on its proposal for listed companies to be required to disclose the proportion of women on their boards and in the company as a whole, and expects that related changes to the Code will become effective in April 2013.

It is clear that the governments of European Union member states are taking a variety of different approaches in an attempt to address the issue of gender diversity on boards. While the introduction of quotas for women on boards remains a controversial topic, several EU member states, including Belgium, France, Italy, the Netherlands and Spain, have moved to adopt legislation introducing mandatory gender quotas.

Following in-depth debates in Germany during 2010 on the proposed implementation of similar mandatory quotas, the Government Commission on the German Corporate Governance Code (the German Code) announced that it sees no need for any alterations to the German Code in 2011. Further, it emphasised its reluctance to make further amendments to the German Code before listed companies have been allowed a reasonable and realistic amount of time to implement the 2009 amendments to its rules. The Commission applied this in particular to the recommendation to increase female representation on boards that was introduced in 2010, pointing towards the large number of women recently appointed to supervisory board positions of Germany's DAX 30 companies and its expectation that the degree of representation will continue to grow, especially in the spring of 2013 when many of the periodic new elections to supervisory boards are held.

In an alternative to mandatory quotas for all listed companies, other countries – Denmark, Finland, Greece, Austria and Slovenia – have adopted rules on gender balance for the boards of state-owned companies. In a softer variation, the UK government has set itself an 'aspiration' that women will comprise 50 per cent of all new public appointments by 2015.

'Comply or explain'

There has been increasing recent focus on the use within Europe of the 'comply or explain' principle, which has been applied in the UK for several years and, more recently, implemented by an EU directive throughout the EU. Under the principle, companies must either comply with the requirements of the applicable corporate governance code or explain the reasons for non-compliance. In its Green Paper, the Commission has indicated two perceived shortcomings in applying the principle in EU member states; first, the provision by companies of inadequate 'explanations' in the event of non-compliance, and second, insufficient authority on the part of the applicable regulatory bodies to monitor this disclosure and require companies to complete insufficient explanations. Other critics of the regime have often also pointed out that, in many jurisdictions, the majority of companies opt to comply, rather than explain, which reduces the utility of having an option to 'explain' and can result in compliance which may apply the 'letter', but not necessarily the 'spirit', of the code.

Responses to the Green Paper have not strongly supported the proposal that regulatory bodies have greater authority to check the quality of the explanations in governance disclosures and require their completion. Most respondents deemed investors, boards, auditors and other stakeholders as adequate contributors to that role and others saw it as incompatible with the comply or explain principle. There is, however, growing pressure within Europe on appropriate investor scrutiny of explanations against compliance with corporate governance codes and the majority of responses to the Commission's consultation paper were in favour of ensuring the disclosure by companies of more detailed and thorough explanations. In the UK, for example, even the FRC – which has strongly defended the comply or explain principle – has indicated that it will be paying 'particular attention' to the quality of explanations and has encouraged investors to highlight examples of good and bad quality explanations.

Shareholder rights and responsibilities; stewardship

Implementation of EU Directive 2007/36/EC (the Shareholders' Rights Directive) by EU member states has continued in 2011 and 2012. Effective from 1 January 2012, Belgium has enacted implementing legislation addressing various rights of listed companies' shareholders (some of which also apply to non-listed company shareholders). The changes are generally designed to improve the information rights of company shareholders, permit shareholders to participate in shareholder meetings by electronic means and otherwise facilitate shareholders' participation in meetings. Importantly, the revisions allow shareholders holding, individually or jointly, at least 3 per cent of the share capital of a company to: add items to the agenda of the company's shareholder meeting; introduce various provisions governing companies' obligations to deliver information and company documents to shareholders, free of charge on request, and to provide certain minimum information via its website or in the shareholder circular; and introduce a mandatory record date system.

In light of the ongoing focus on the stewardship role of investors and on improving investor engagement, the Green Paper solicited feedback on a number of questions on how to encourage shareholders to take an interest in sustainable investment returns and long-term company performance in an attempt to counter short-term investment models and the associated impact that they can have on governance. Respondents demonstrated support for the implementation of a technical or legal European mechanism to help companies identify their shareholders in order to facilitate dialogue on corporate governance issues; for example, through lowering the thresholds for notification of major holdings in the EU Transparency Directive so companies better understand who their shareholders are.

The Green Paper also asked whether measures should be taken on the incentive structures and performance evaluation of asset managers managing long-term institutional investor portfolios to encourage them to seek long-term benefits (which, according to the Commission, is more likely to lead to a long-term governance approach). There was generally not strong support for this proposal. Most respondents against it pointed out that these types of measures are for the parties to the asset management arrangements to negotiate and decide and some respondents pointed to the UK's Stewardship Code as a more effective means of addressing these issues. The Stewardship Code, published in 2010, requires institutional investors with managed assets to have and disclose a policy on how they will discharge their stewardship responsibilities with respect to investee companies, their policy on voting and disclosure of stewardship and voting activities.

Asia

In recent years, there have been considerable developments in corporate governance standards applicable to companies listed on the Hong Kong Stock Exchange (HKEX) and the HKEX has now adopted its extensive proposed changes to the corporate governance code and listing rules, most of which took effect in early 2012. Aside from Hong Kong, however, the pace of change in improving governance standards elsewhere in Asia generally remains slow. But the need for reform has been highlighted and investors' concerns over the pace heightened in light of the recent issues surrounding Olympus, whose governance, accounting and compliance failings very nearly resulted in it being delisted from the Tokyo Stock Exchange (TSE) in December last year.

Japan

In a series of developments in 2011 beginning with the termination of its chief executive in October, a number of deficiencies in the governance, internal controls and financial reporting procedures were identified at the Japanese camera company Olympus in recent months. In particular, Olympus was found not to have reported significant financial losses for over two decades, and was required to re-file its earnings disclosure with the TSE. Deficiencies in the implementation of its employee whistleblower procedures were also identified. While it has not been delisted, Olympus' stock is 'on alert' by the TSE, requiring it to submit annual reports to the TSE on how its corporate governance and internal controls are being improved.

These issues have served only to focus attention further on the need for reform of the governance standards applicable to listed companies in Japan – particularly, a need for increased accountability and transparency, for procedures to avoid conflicts of interest between shareholders and corporate executives and for the adoption of higher board independence requirements. Further to its ongoing discussions on revisions to the Companies Act to improve governance standards, the Japanese Ministry of Justice published its Interim Proposal regarding proposed revisions in December 2011.

The Interim Proposal is for public consultation purposes and because, on each topic, it includes a number of alternative proposals, it is difficult to estimate at this stage what the ultimate package of revisions would look like. That said, one of the key proposals would amend the Companies Act to require the appointment by all listed companies of at least one independent outside director, although concerns have been expressed that a minimum of one director is not sufficiently high and that the proposed definition of independent is too narrow to be aligned with international governance norms. There are also other areas where the Interim Proposal does not extend as far as standards in other developed markets – for example, in not requiring fully independent audit committees with formal and regular oversight over financial reporting, internal controls and risk management, internal audit and external audit. The public consultation period on the Interim Proposal has recently ended and it is not yet clear what the next steps will be or which combination of these proposals – if any – will become law.

Hong Kong

Following considerable regulatory discussion in Hong Kong on governance standards and after more than a year's work, in October 2011 the HKEX published the conclusions of its consultation paper on its review of the Hong Kong Corporate Governance Code (the HK Code) and the HKEX Listing Rules Code. Most of its extensive proposed changes to the HK Code and Listing Rules were adopted and took effect in January and April 2012. One of the key changes to the Listing Rules – the requirement that independent non-executive directors (INEDs) comprise one-third of a listed company's board – will take effect on 31 December 2012, and new Listing Rules requiring a mandatory 15 hours' of professional training in each financial year for company secretaries will take effect on a staggered basis according to the date of appointment of an individual as company secretary.

A significant number of the revisions are directed at the main actors in the implementation of corporate governance – the directors and the company secretary – and the constitution and responsibilities of various committees of the board. In respect of directors, the revisions generally are designed to heighten the level of active participation required from directors such that mere attendance at board meetings is not sufficient. The changes also address the need for greater independence requirements for remuneration and nomination committees.

Many of the changes have been implemented on the basis originally proposed. In other cases, the HKEX has amended its original proposals to reflect feedback received from respondents to its consultation. Some of the main changes include:

- reducing certain proposed requirements from the level of a binding Listing Rule to a HK Code provision (subject to comply or explain) – such as the requirements that companies disclose the remuneration of all senior management by band;
- eliminating its proposed upgrade of the 'recommended best practice' (with which companies are simply encouraged to comply or explain) of performance-linked compensation for executive directors to a Code provision;
- eliminating its proposed cap on the number of INED positions that an individual may hold, although the proposed requirement for a shareholder vote on the reappointment of an INED who has served for more than nine years has been adopted;
- deletion of its recommended best practice that listed companies establish corporate governance committees; instead including a HK Code provision that the board should be responsible for performing its enumerated corporate governance duties and a Listing Rule requiring disclosure of the performance of governance duties.

All in all, 2011 has been a year of progress – in some countries and areas perhaps not enough, and in others, perhaps a 'lack' of progress has been the best result.

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