

Corporate Governance Update

Asia

Convergence and divergence in corporate governance codes

“The issue of which models of corporate governance is right for emerging markets has become a highly sensitive one. It is widely believed that ‘one size doesn’t fit all’, meaning North American and Europe should not seek to impose their standards on developing economies and that an international code of best practice is unworkable. Legal systems, business cultures and corporate structures are just too different, even among developed nations.” A paper by Jamie Allen, Secretary General of the Asian Corporate Governance Association, identifies the points of convergence and divergence between practices in eleven Asian countries.

Source: Corporate Governance International, Hong Kong Institute of Company Secretaries, Sweet and Maxwell, Hong Kong, Volume 3 Issue 1, March 2000

Canada

Corporate governance and director compensation

In their sixth annual review of corporate governance and director compensation, Patrick O’Callaghan and Associates, highlight a number of significant changes in the 1999 data. 61% of the surveyed companies now include a stock based element in their director compensation plan, up from 22% when the survey began in 1993. The number of companies with at least one woman director has risen from 46% last year to 50%. However 65% of the companies surveyed failed to indicate whether their governance practices matched the Toronto Stock Exchange guidelines. 53% of companies surveyed now have a process for assessing individual director competence.

Source: Patrick O’Callaghan and Associates; Corporate Board Governance and Director Compensation in Canada, a review of 1999, 999 West Hastings

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China

US shareholder activism thwarts IPO by PetroChina

The labour organisation AFL-CIO Office of Investment set up a web site to warn of corporate governance deficiencies in a proposed IPO by PetroChina, the largest oil company in the People’s Republic of China, controlled by the Chinese government. The risk factors outlined related to PetroChina’s governance structure, ethical issues regarding alleged human rights abuses in Suan and Tibet, and the expected lay-off of a million workers in China. The campaign by AFL-CIO included calls to more than 50 investment managers, warning that “they would be well-served to avoid this issue, as it is virtually impossible to perform due diligence on the company since the underwriters cannot verify what they are told. The IPO, though not cancelled, failed to attract the funds expected. Other planned listings have been delayed.

Source: IRRC Corporate Governance Bulletin; February–April 2000, Volume XVIII number 1. Suite 700, 1350 Connecticut Avenue, NW Washington DC 20036, USA

Germany

US shareholder activism attempts to thwart Vodphone/Mannesman merger

In another example of the new global activism of the AFL-CIO Office of Investment (see above item on China) investment managers were told of the ‘harmful strategic implications’ of the merger. The AFL-CIO believes that the European model of corporate governance, which seeks consensus between labour and capital, is the better model and creates more long-term value for shareholders. Germany’s largest union, IG Metall also

sought to block the merger, which in the event was completed.

Source: IRRC Corporate Governance Bulletin; February-April 2000, Volume XVIII number 1. Suite 700, 1350 Connecticut Avenue, NW Washington DC 20036, USA

Common principles of corporate governance in Europe?

"The convergence of the common law and the civil law is an old dream – or nightmare – an outlook that depends on which side of the Channel the idea is held, and more on how international the outlook if the academic or practitioner." Thus Professor dr. Klaus J. Hopt begins his contribution to the Clifford Chance Millennium Lectures. The paper is not strictly comparative, focusing on the influences of British law and corporate governance on German and European law, rather than the influences of the later on British law. In a scholarly analysis of the differences between two-tier and unitary board regimes, he concludes that there has already been, and will be more, convergence between the Anglo-Saxon and Continental European countries in the fields of corporate and capital market law, and specifically in corporate governance.

Source: Common Principles of Corporate Governance in Europe? The Clifford Chance Millennium lectures – the coming together of the common and the civil law, Hart Publishing, Oxford, England and Portland Oregon, 2000

Greece

Principles of corporate governance launched

The Capital Market's Commission of Greece has released a set of Principles of Corporate Governance, modelled on the OECD code. Best practices in corporate governance advocated include an end to multiple-voting shares, a limitation on board size to 13, audit and remuneration committees, executive director pay tied to performance and the splitting of chairman and CEO posts.

Source: Global Proxy Watch and IRRC Corporate Governance Bulletin, November 1999-January 2000

Hong Kong (Special Administrative Region of China)

Rules on the Growth Enterprise Market (GEM) relaxed

The Hong Kong Securities and Futures Commission (HKSCF) and the Hong Kong

Stock Exchange have relaxed the listing requirements for companies on the GEM. Initial shareholders would now be locked in for six months, rather than two years (with some restrictions preventing changes of control). The requirement for active business pursuits and accountants reports would be for one year, rather than two. Restrictions on share options were also relaxed. The rationale for the changes was to bring the GEM into line with international competition. Critics argued that the level of protection offered by the GEM was less than that of other, competitive markets. The power of the HKSCF to ensure regulatory enforcement is limited and concerns are heard of its increasing response to political pressures.

Source: South China Morning Post 10 – 14 March 2000

Investor activism in the HKSAR

As Chairman of the Investor Responsibility Taskforce of the new World Bank/OECD initiative – the Global Corporate Governance Forum – Mark Mobius commented "corporate governance is in a very sad state, not only in Asia but globally. The problem of multi-lateral organisations, such as the World Bank and the OECD, is that they are not willing to commit themselves to action. They don't pinpoint individual cases of violations of shareholder rights because they do not want to step on any toes. Meanwhile we are getting ripped off."

As the head of Templeton Emerging Markets Fund, Mobius, further commented "small investors know that they will be listened to less than the big money, so (they) tend to sell and get out. (But) large pension funds, such as CalPERS, Hermes and ourselves, realise that we have so much invested that we cannot get out rapidly... which is one of the reasons we have become more active in recent years... many fund managers adopt the mentality of 'shareowners' rather than 'shareholders'. Many are predicting that these new advocates of corporate governance values have a better chance of succeeding where governments and a whole panoply of multilateral institutions have failed."

Source: Company Secretary (Hong Kong) March 2000 Volume 10 no. 3

Ratio of companies to population very high

On 1 January 2000 Hong Kong had 490,888 registered companies, of which 6,058 were public. This gives the SAR one of the highest

ratios of companies to head of population in the world, with one company for every 13 people.

Source: Company Secretary (Hong Kong) March 2000 Volume 10 no. 3

Standing Committee reject consultant's recommendations

A review of company law was instituted in 1994. Consultants were appointed, who reported in 1977. Now the Standing Committee on Company Law Reform has reacted to that report and made their proposals for change. Whilst accepting many of the detailed proposals, their report rejects two fundamental proposals from the consultant: namely that the companies ordinance should be replaced with a new statute built on North American models (Revised Business Corporations Act and the Canada Business Corporations Act); and that the role of company secretary should be dropped.

Source: Hong Kong Report of the Standing Committee on Company Law Reform – on the recommendations of a consultancy report of the review of the Hong Kong Companies Ordinance February 2000

India

New corporate governance code

The Securities and Exchange Board of India has developed a corporate governance code, recommending the use of independent outside directors, with one half being outside directors and one-third independent. Also recommended are the separation of board chairmen from chief executive officers, better board procedures and accounting standards and financial reporting, and the use of audit and remuneration committees.

Source: IRRRC Corporate Governance Bulletin, November 1999-January 2000

International

OECD Principles of Corporate Governance

The non-binding principles, based on experiences from various initiatives in member countries, are intended to assist member and non-member governments in their efforts to evaluate and improve the legal, institutional and regulatory framework for corporate governance in their countries, and to provide guidance and suggestions for stock exchanges, investors, corporations, and other

parties that have a role in the process of developing good corporate governance. The principles are available in HTML and can be downloaded in PDF format. Alternatively order through the OECD bookshop.

Source: <http://www.oecd.org/daf/governance/principles/htm>

The governance of dotcom companies

“The governance issues raised by dotcom companies derives from their Janus-faced character – on the one hand, they combine the market valuation of a blue-chip S&P 500 company; on the other, their boardroom suggests a venture capital funded start-up. At companies such as Yahoo! and PSINET, half the board members are executive insiders, creating situations where management is permitted to oversee itself unencumbered by the vigilance of an independent board”

Source: Governance, the international corporate governance newsletter, Issue 77 March 2000
<http://www.governance.co.uk>

Employee ownership expounded in new website

The Foundation for Enterprise Development offers a range of advice and experience to companies contemplating employee ownership schemes or the development of existing programmes. Advice on equity-sharing and equity-incentive schemes is available on-line.

Source: <http://www.fed.org>

ERaider.com offers an Internet opportunity for dissatisfied shareholders to unite

A web site, which describes itself as a ‘confederation of shareholders who believe that owning a company carries rights and responsibilities,’ plans to use the Internet to help individual shareholders, dissatisfied with the performance of a company in their portfolio, to bring collective action against the company. The organisers hope to be able to give new power to small investors in the corporate governance battle. (The web site has pirates, cannons and cutlasses to support this aggressive and confrontational approach).

Source: Governance, Issue 79 May 2000. Watchfield House, Watchfield, Highbridge, Somerset TA9 4RD T 44 1278 793 300 F 44 1278 783 750
<http://www.governance.co.uk>

New ethical portfolio manager

Data on almost 2,000 US, UK and Continental

European companies are included in a new software programme, focussing on ethical, social and environmental policies and practices. Based on 17 years experience of developing relevant performance indicators, this programme enables portfolios and company's risk and reputation to be analysed. Windows 95 or above.

Source: Eiris, Ethical Portfolio Manager, 80-84 Bondway, London SW8 1SF, UK T44 20 7840 5710 F 44 20 7735 5323

Japan

A shifting emphasis from stakeholder to shareholder

In a briefing note for a newsletter of the Institute of Chartered Accountants in England and Wales, Dr. Loizos Heracleous writes that post-war corporate governance in Japan was based on extensive interlocking directorates among networks of firms called *keiretsu*. These firms engaged in reciprocal trade, relational contracting, management exchanges, information sharing and often selective intervention to rescue firms in danger of collapsing, especially by banks central to the network. Corporate governance was characterised by a stakeholder orientation...corporate goals were oriented mainly towards survival, growth and stability as opposed to an explicit focus on profitability and shareholder value...an active takeover market or pressures from institutional investors were absent or not functioning well. However, a number of concurrent trends have brought significant pressures on this stakeholder-oriented system. Firstly, Japanese banks at the centre of *keiretsu* have weakened financially, as reflected in their credit ratings. Worsening economic performance has induced *Keiretsu* firms to sell their cross-shareholdings. Institutional investors from the West began to pressure Japanese companies to improve shareholder value. The emphasis of corporate governance in Japan has thus shifted from a wider stakeholder orientation to a more explicit shareholder orientation, and has prompted substantial board restructurings and the use of incentives for directors. What remains unaddressed is the inclusion of a strong independent element on the board...non-executive directors, in the sense commonly understood in the West, are scarce on Japanese boards.

Source: Dr. Loizos Heracleous, School of Business Studies, Trinity College, Dublin, Ireland T 353 1 608 2312 F 353 1 679 9503 e-mail heraclel@tcd.ie

Mexico

A new Corporate Governance Code has been introduced. Jointly drafted by the Mexican Stock Exchange, the Mexican Bankers' Association, the Mexican Institute of Financial Executives and the Mexican Institute of Public Accountants, the code is voluntary but firms are required to report compliance to the Exchange. This is the first code of its kind in Latin America.

Source: IRRC Corporate Governance Bulletin, November 1999–January 2000

Russia

OECD Conference on shareholder rights

In Russia, corporate governance is even more important than in other transition and emerging economies. Low levels of market confidence and weak institutional infrastructure make corporate governance at corporate level the principal defining factor in the availability of foreign investment. More importantly, improvements in corporate governance are intimately linked to an overall improvement in the rule of law; ineffective corporate governance is generating corruption and low respect for the law at most levels in private and public life. Part of a three year programme, an OECD/World Bank Corporate Governance Roundtable was held earlier this year. Some 80 government and private sector representatives from Russia and other OECD countries, reviewed the rules, procedures, practices and institutions for ensuring shareholder rights and equitable treatment in Russia. Russian blue-chip companies were invited to share their experiences on shareholder relations with regulators and investors. Policy recommendations and efforts for reform were outlined, using the OECD Corporate Governance Principles were used as the conceptual framework (see the International section above).

Source: <http://oecd.org/news>

South Korea

A Corporate Governance Reform Committee has called for firms with capitalisation of over 1 trillion won (US\$900 million) to have at least 50% independent members on their boards. It also recommends the use of audit, nomination and remuneration committees comprising predominantly outside directors.

Source: Global Proxy Watch and IRRC Corporate Governance Bulletin, November 1999–January 2000

Thailand

New listing rules requiring audit committees

The Stock Exchange of Thailand (SET) has introduced new listing rules requiring listed companies to have audit committees made up of independent directors, with at least one having financial expertise. The SET also encourages the use of independent directors, recognising the problem frequently found in Asia Pacific boards comprised of directors connected with the major shareholder or family interests.

Source: IRRRC Corporate Governance Bulletin, November 1999-January 2000

United Kingdom

Crucial stage in company law review

The review of company law in Britain has reached a critical stage with the publication of a massive 462-page report. This follows the first consultation exercise – reported earlier in these columns. Most respondents sought to retain the sole accountability of companies to shareholders but in a more ‘inclusive’ way (however that might be interpreted). In a series of chapters on aspects of corporate governance, the report considers directors and officers (restating directors’ duties, with an inclusive duty of compliance and loyalty plus an objective duty of skill, care and diligence), shareholders (improving the relationship between company and its members; but AGMs will still be required), reporting and accounting for large companies (the preliminary statement of results should be a statutory document available on a website; major companies should also report on operating matters to enable the user to assess the performance of the business and its wider relationships with stakeholders [although that word is not used]), issues for small and private companies (proposing more simplification) The Review was set-back last year when David Wheeler, of the Body Shop, and an advocate of stakeholder inclusive and environmentally friendly responsible perspective, when the committee decided to drop the notion of stakeholder rights in favour of the old model, with shareholding as the basis of power. In their response to the document, the Institute of Chartered Secretaries and Administrators (ICSA) calls for company secretaries to be retained. The report’s proposal to dispense with company secretaries in private companies “would be contrary to all principles of corporate governance.”

Source: Modern Company Law- for a competitive economy; Developing the Framework, a consultation document from the Company Law Review Steering Group, March 2000.

<http://www.dti.gov.uk/cld/review.htm>

Source: The Ethical Investor, January/February 2000 80-84 Bondway, London, SW8 1SF

Source: Press release from the ICSA, 19 June 2000 Robert Banks T 44 20 7580 4741

Proxy voting by Internet becomes a reality

Previously prevented by company law, the government’s Electronic Communications Act, supported by detailed regulations from the Department of Trade and Industry, will permit electronic voting on company resolutions, the delivery of corporate reports electronically and the use of electronic signatures.

Source: Governance, the international corporate governance newsletter, Issue 77 March 2000 <http://www.governance.co.uk>

Major pension funds adopt ethical investment policies

The University Superannuation Scheme (USS), the pension fund for university staff and the third largest fund in the UK, is strengthening its socially responsible investment policies. The USS joins the British Telecom pension fund and the British Coal fund in its commitment to ethical investment. The USS has appointed new staff to monitor companies and will take up ethical matters with those companies. They also list all the companies in which they invest on their web site.

Source: ERIS Ethical Investor March/April 2000 <http://www.ussq.co.uk>

The non-executive directors’ view of risk

Some boards are now setting aside time to consider aspects of risk and its management. One company explores each individual director’s perception of risk. Despite the Turnbull report’s emphasis on internal controls, they found that the outside directors were more concerned about exposure to external risks. Some pertinent comments emerged from one director:

1. There is a risk that a top-down assessment of risk and control, emanating from the group board, will overlook key risks within individual businesses of the group.
2. There is a real risk that the focus on ‘top-down’ assessment of risk will overlook major risks and control weaknesses, which may be concealed in the systems of the business.

3. One of the risks a business faces is the loss of stakeholder confidence that the board really knows what is happening within the business.
4. Does the company have the competencies it needs, now and in the future? Do we know what our key competencies are?

Source: Internal Control, Issue 30 April 2000, ICAEW, ABG Professional Information, PO Box 21375, London WC1N 1QP T 44 20 7920 8991 F 44 20 7920 8992 www.abgweb.com

Check list for joining a board

The full implications of becoming a company director challenge many people. What can you bring to the board? What is the personal risk? Consider the compensation package and the tax implications. In a private company do the shareholders agree? How to learn about the company? What skills and time commitment is needed? Is the board really in charge? What about succession planning, financial and management accounting matters, the conduct of board meetings? Useful insights can be found in this checklist before joining a board.

Source: Corporate Governance, March 2000, Issue 2, Chartered Association of Certified Accountants; Editor, Andrew Chambers, Management Audit Ltd. 6, Market Street, Sleaford, Lincs., NG34 7SF, UK <http://www.management-audit.com>

Yet another publication titled 'Corporate Governance'

The Institute of Chartered Accountants in England and Wales has launched a newsletter titled 'Corporate Governance', adding to the many with that name in the publications index. Aimed at professionals involved with performance accountability and the management of risk, the focus will be on an international update on current developments. The 10 annual issues will reflect the renewed interest in corporate governance following the UK Turnbull Report.

Source: ABG Publications, 40 Bernard Street, London, WC1N 1LD, T 44 20 7920 8991 <http://www.abgpublications.co.uk>

Cyber police target web share fixers

Several mergers and takeovers have been first revealed on websites. Now the Financial Services Authority (FSA), the City regulator, has clamped down on those spreading misleading rumours or insider information through Internet bulletin board or chat rooms.

The FSA has discovered many pieces of potentially fraudulent information. Three types of cyber crime have been identified. First, touts paid by companies to pump up their share values through Internet bulleting boards. Second, the spreading of insider information through chat rooms. Third, potentially the most common, 'pumping and dumping' in which fraudsters, holding shares provide false information to tempt unwitting buyers who pile in, the price rises, the fraudsters sell and the price collapses.

Source: The Times, 9 April 2000

The Corporate Governance Special Interest Group

The Corporate Governance Special Interest Group of the British Accounting Association continues to develop. The fourth issue of their newsletter (February 2000) contains useful information and calls for papers on relevant conferences around the world.

Source: <http://www.shef.ac.uk/~baacgsig>

Corporate governance in public and voluntary bodies

The RSA (Royal Society for the Encouragement of Arts, Manufactures and Commerce) has launched a project on the governance of public and voluntary bodies, following a conference of interested parties in January 2000. A Steering Group is now focusing on the roles of governing bodies of both public and voluntary bodies – boards of trustees, councils, committees etc. The National Audit Office has played an important role in the project through its White paper 'Modernising Government', which emphasises the importance of risk management and focusing on outputs. The Steering Group will undertake a survey of corporate governance needs in the public sector and prepare a comparative analysis of needs in the voluntary sector. Crucial questions will include what messages can be gleaned from corporate governance developments in the private sector, what is the link between authority and responsibility in the public sectors (particularly in health and education, and in quasi-governmental agencies and non-departmental government bodies) and what are the critical corporate governance issues in the voluntary sector?

Source: RSA notes from the conference held at Leigh Court, Bristol, 11 January 2000. RSA Leigh Court, Abbots Leigh, Bristol, BS8 3RA. T 44 1275 371145 F 44 1275 371146 <http://www.sage-rsa.org.uk>

Directors' indemnity insurance

The importance of indemnity insurance, long recognised in the United States, has recently been emphasised by the UK Institute of Directors (IoD). In addition to the risk of civil damages, directors in the UK can be at risk under the provisions of the Companies Act 1985, the Insolvency Act 1986, the Financial Services Act 1986, the Fair Trading Act 1973, the Company Directors Disqualification Act 1986, the Health and Safety at Work Act 1974, the Data Protection Act 1984 and others. The IoD have endorsed a Director's Personal Indemnity Insurance package from Chubb Insurance (Europe) s.a. Chartered members of the Institute and holders of its diploma receive discounts.

Source: Institute of Directors, 116 Pall Mall London, SW1Y 5ED

UK companies producing social reports and a new standard

14 of the top 100 companies in the UK now produce a social report, responding to the interests of various stakeholders, not just the shareholders. The social auditors association AccountAbility has launched a new standard AA1000, which gives internal and external stakeholders reassurance that there is substance behind a company's actions not just PR.

Source: The Ethical Investor, January/February 2000 80-84 Bondway, London, SW8 1SF

United States*SEC brings first case against Internet share fraudsters*

The Securities and Exchange Commission (SEC) has brought the first case against Internet share fraudsters. Nineteen people were charged of making illegal profits from passing insider information. The scheme was uncovered when the Innermarket Surveillance Group at the American Stock Exchange noticed unusual trading prior to public announcements to the SEC. Only three of the 19 people actually used the Internet to pass information. The perpetrator of the fraud, employed by a temporary word-processing service, worked at two leading Wall Street brokers, where he learned of 23 merger and acquisition transactions. The SEC is trying to build an Internet search engine that will scan bulleting boards for suspicious share information.

Source: The Times 9 April 2000, Seattle Times 19 March 2000

New audit committee requirements from the SEC and the US stock exchanges

Following the 1999 recommendations from the Blue Ribbon Committee on improving the effectiveness of corporate committees, the SEC have approved rule changes from the NYSE, the AMEX and NASDAQ exchanges intended to improve audit committee effectiveness, enhance disclosure about audit committees and strengthen the reliability of financial statements, through information on audit committee composition and charter. New SEC rules require specific information in the audit committee report and on the independence of audit committee members.

International Corporate Governance Network

The fifth annual conference of the International Corporate Governance Forum was held in New York in July 2000. A related conference on the shareholders' role in corporate governance in emerging and transition economies was held at the Connecticut State University, sponsored by the World Bank/OECD Global Corporate Governance Network, the Asian Corporate Governance Association, the Commonwealth Association of Corporate Governance, the Brazilian Institute for Corporate Governance and Davis Global Advisers.

Source: organisers' material July 2000

Two firms adopt shareholders' alternative voting information (SAVI)

This column has previously noted the SAVI (pronounced 'savvy') proposal, developed by Mark Latham, in which shareholders of a widely held company would vote to hire a proxy advisory firm to give shareholders independent information and a more powerful voice in corporations. The idea is being voted on at two companies – Whole Foods Market (WFMI) and Washington Mutual (WM).

Source: <http://www.corpmon.com>

Chairman of SEC questions audit firm independence

Arthur Levitt, Chairman of the US Securities and Exchange Commission has raised some significant questions: "Should there be more appropriate limits on the types of services that an audit firm can render to a public

company client? How should audit firms be structured to assure independence? What are the consequences, if any, of public ownership? Should firms be permitted to affiliate with entities who provide services to the firm's audit clients that the firms themselves would not be allowed to provide?"

Source: Speech given by Arthur Levitt to The Asia Society, Hong Kong. See <http://www.sec.gov> and the Company Secretary, Hong Kong Volume 10 number 6 June, 2000

CEO contracts published on the Internet

The contracts of more than 250 US chief executives have been published on the web site of the corporate library, run by Nell Minow and Bob Monks (members of the Editorial Advisory Board of this journal). The best contract, according to the survey, was that of Jack Welch, renown head of General Electric). Others were less acceptable, including those that provided massive remuneration however disastrous the company performance, and one which provided the CEOs mother with first class air travel and more!

Source: Governance, Issue 78 April 2000 and see <http://www.thecorporatelibrary.com>

1999–2000 US board practices and compensation survey

The latest survey by Russell Reynolds and IRRRC, based on responses from over 1,200 companies listed on the S&P 500, Midcap 400 and Smallcap 600, shows some significant trends in director remuneration. Almost one half of companies listed on the S&P 500 now grant annual options to directors (an increase of 50 percent over 1995 levels). Only 10% of S&P 500 company boards offer retirement benefits to directors (a decrease from 61% in 1995). The number of board committees monitoring corporate governance issues continues to grow; more than 50 percent of the S&P 500 now have a committee responsible for reviewing corporate governance issues (up from 11 percent four years ago).

Source: 1999-2000 Board Practices Survey – the structure and compensation of US public companies, Russell Reynolds, Suite 2300, 200 Park Avenue, New York 10166-0002, USA F 1 212 370 0896

"I don't agree with Sir Adrian Cadbury that the first priority of the non-executive is to be a check and balance and a monitor. Their primary task is to come on and see the wood for the trees, to help people make correct business-judgement decisions."

Mervyn King, chairman of the King Report on corporate governance in South Africa (1994) quoted in Governance, Issue 78 April 2000

"There is nothing quite like the notion of 'independence' to rattle the timbers of the non-executive director. To pin it down is like nailing a jelly to the ceiling."

Andrew Chambers, Editor, Corporate Governance – for prosperity and accountability
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