Statement of the European Corporate Governance Forum on Cross-border issues of Corporate Governance Codes

1. In its statement on the comply-or-explain principle of 22 February 2006, the Forum expressed its concerns about the application of corporate governance codes in cases where a company is incorporated in one Member State and its shares are listed in one or more other Member States. Sometimes this may lead to a double application of corporate governance codes in two jurisdictions, in other cases it may lead to the result that no corporate governance code is applicable to a particular listed company.

2. The critical factor leading to these results is the differing legal bases for the codes and for the obligation to comply with a code or to explain deviations. Sometimes this obligation is based in company law, for example in the case of the Netherlands and Germany, requiring companies incorporated in that particular Member State to comply with the code of that state, typically irrespective of where the shares of the company are listed. In other cases this obligation is laid down in securities listing rules, for example in the case of the UK and Sweden, requiring companies with a primary listing on the stock exchange in that Member State to comply with the code of that State, irrespective of where the company has been incorporated. Finally, some Member States have not designated any specific code to which the comply-or-explain obligation relates or have not any such comply-or-explain obligation on listed companies, like France.

3. As a result, for example, a company incorporated in the Netherlands or Germany, with its primary listing in Sweden is subject to the Dutch or German Corporate Governance Code (applicable to companies incorporated in the Netherlands or Germany with a share listing on any regulated market) as well as the Swedish or UK Code. On the other hand, a company incorporated in Sweden or the UK with its primary listing in the Germany or the Netherlands is neither subject to the Swedish or UK Code nor to the Dutch or German Code.

4. Directive 2006/46 amending the 4th and 7th Company Law Directives introduced a new article 46a in the 4th Directive, requiring a company whose shares are admitted to trading on a regulated market, to include a corporate governance statement in its annual report. This statement amongst others should include a reference to the corporate governance code the company is subject to or has decided to apply and the extent to which the company departs from such code and the reasons for doing so. To the extent the company departs from that code, it shall explain of which parts of the code it is departing and the reasons for doing so. Where a company has decided not to apply any provisions of such code it must explain its reasons for doing so.

5. Article 46a does not impose an obligation on Member States to designate a code that listed companies must apply. Nor does it deal with potential double application of codes from two jurisdictions or the absence of applicability of any code that may result from cross-border (multiple) share listings. The Forum believes that this is undesirable. The Forum believes that companies incorporated in the EU the shares of which are admitted to trading on a regulated market should at least apply one code and should not materially have to apply more than one code. In order for this to come about, the Forum recommends the introduction of two new rules.

(1) A requirement for companies incorporated in the EU of which shares are traded on a regulated market to apply (i.e. comply or explain) a corporate governance code applied in either the Member State of its registered seat, or the Member State of its primary share listing. Where the company is incorporated and its shares are traded on a regulated market in the same Member State, no issue arises. Where they are different, the company should choose which of the two codes it applies.

(2) A Member State should require no more than that a company that is either registered in that Member State or the shares of which are admitted to trading on a regulated market in that Member State, but which applies another Member State's corporate governance code (because either it is registered in that other Member State or its shares are admitted to trading in that other Member State) explains in what significant ways the actual corporate practices of that company deviate from those set out in the Member State's corporate governance code.

6. This second rule is already applied in the UK Listing Rules (LR 9.8.7), providing:

> An *overseas company* [i.e. not UK incorporated] with a *primary listing* [in the UK] must disclose in its annual report and accounts: (1) whether or not it complies with the corporate governance regime of its country of incorporation; (2) the significant ways in which its actual corporate governance practices differ from those set out in the *Combined Code*; and (3) …[1]

Similarly, the New York Stock Exchange, exempts foreign private issuers from application of its Listing Standards on Corporate Governance, but requires them to disclose any significant ways in which their corporate governance practices differ from those followed by US domestic companies under the NYSE Listing Standards (303A (11)).

7. The benefit of the first suggested rule is that a company with a cross-border share listing has the freedom to choose which of two potentially applicable codes it wishes to apply, in light of its own particular circumstances, company law organisation, shareholder base, governance traditions etc., but that it must at least choose either the code of the Member State of incorporation or the code of the Member State where its shares are admitted to trading on a regulated market. The second rule then avoids the double application of two potentially applicable codes, but requires that significant ways in which the actual corporate practices differ from those provided for in the code which is not applied are disclosed. Shareholders are still fully informed, without the double application of two codes.

[1] A proposal to amend this provision has been published by the FSA in December 2008, requiring an overseas company to disclose the corporate governance regime to which it is subject, whether or not it complies with that regime, an explanation of the main ways in which its corporate governance regime differs from the Combined Code and the extent to which it complies with those provisions of the corporate governance regime to which it is subject that correspond with the Combined Code, and if it does not comply with any such provisions, an explanation of why it does not comply.