

holders represented on the other hand. An important part of the dialogue remains bilateral and is not vented in the marketplace.

At the time of the annual general meeting (AGM), the shareholders have to take a certain number of decisions, which are far from being formalities. The election or the re-election of members of the board of directors, modifications to the statutes and even granting the discharge to the responsible bodies can involve major issues, as can shareholders' proposals. In Switzerland, the majority of listed companies have uneventful AGMs, which is not the case in every country. In the U.K., for example, remunerations are submitted to an advisory vote. In Germany, alternative candidatures for the board of directors are a reality. Even in Switzerland one can remember that in the recent past the discharge was refused within a company like SGS or that Nestlé barely refused a shareholders' motion to prohibit dual mandates.

The AGM also provides an opportunity to speak publicly to the assembly of shareholders. According to Swiss law, shareholders have the right to ask questions. Those which were not answered in bilateral discussions can be asked at the AGM, so that they are shared with the shareholder community. The votes also provide the opportunity to give voting recommendations, which are particularly important for value-based shareholders, since their goal is to convince a majority and not to carry out a tactical manoeuvre aiming at rapid profit taking. This is the reason why ACTARES, for instance, presents its voting positions on its website.

Is it necessary to mention that the recourse to the law courts always remains available to the shareholders when they are convinced that their rights are not respected? In spite of the discretion in this field, many cases become public. It is the ultimate stage of a divergence between the shareholder and the company leadership.

In conclusion, one can retain that shareholder activism should increase in the years to come. However, since it is not a homogeneous movement, it may lead to a certain politicisation of the economy. Companies will have to adjust to this situation and to develop the fiduciary side of their management approach. Leaders who will be able to take intelligent advantage of this situation to improve their vision of the future will give without any doubt a competitive advantage to their company.

ACTARES

ACTARES – Shareholders for a sustainable economy – grew out of the experiences and ideas of two associations of ethical shareholders: the “Convention des actionnaires de Nestlé” (CANES, Convention of Nestlé shareholders), and the “Verein kritischer Aktionärinnen und Aktionäre der Schweizerischen Bankgesellschaft” (Association of critical UBS shareholders). ACTARES provides voting positions for over 20 Swiss companies yearly.

You will find more information about ACTARES under www.actares.ch, info@actares.ch

A plea for pay for performance

Management compensation is one of the most forceful tools to make managers do what investors would like to achieve and receive. Pay for performance – rather than the competitive pay strategy still predominant in Switzerland and other European countries – is best suited to align interests of managers and shareholders.



Pay for performance aligns interests of managers and shareholders.

Stephan Hostettler, Managing Director, Hostettler & Partner AG, Zurich, and visiting professor for Corporate Governance at the University of St. Gallen

It is everything else but a new conclusion that such alignment of interests is a delicate issue. A fair amount of suspiciousness is inherent in the relations between shareholders and managers. It was none other than Adam

Smith, the godfather of economists, who wrote in its “Wealth of Nations” in 1776: “The directors of such companies, being the managers rather of other people’s money than their own, it cannot be expected that they would watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch their own. Like stewards of a rich man, they apt to consider attention to small matters as not for their master’s honour, and very easily give themselves a

dispensation from having it. Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company.” It still is one of the arguments of today’s private equity funds that they run companies more effectively than a public shareholder base because of the better selection and control of top management.

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Others have made the case for the effectiveness of public companies and markets. Today, it is widely believed to be the most effective system in terms of allocation of capital. The selection and control of management, though, has remained one of its problems. Pivotal questions remain: How do the suppliers of finance get managers to return some of the profits to them? How do they make sure that managers do not steal the capital they supply or invest in bad projects? How do suppliers of finance control managers?

A potent way of controlling this, involves the company's compensation scheme to link wealth and salary of top management directly to the long-term value creation – in absolute, not relative terms, neither linked to budgets nor to the implementation of the strategy. As for the latter, direct links between strategy, its implementation and compensation are more often than not a reason for a constant change of the payment criteria. From a shareholder perspective, a fixed, long-term deal with management is more efficient.

It can only be explained by the economist's free-riding theory that not more shareholders of public companies get more actively involved in questioning and shaping incentive and performance schemes. More often than not it is still very much an affair discretely handled by the company's board of directors and top management. Shareholders typically believe in the benefits of free markets and self-regulation. Thus, a general appeal that shareholders themselves should become more active in this process seems to be the appropriate solution. Shareholders should more often question the ways and means how excess returns are being distributed to management, employees and shareholders. Shareholders should stipulate and ask for a minimal return on their investment they expect management to deliver. Shareholders should speak up to receive more information about executive compensation than typically provided by European companies in their corporate governance reports. Shareholders should have a closer look at the mechanics of the salary schemes, and be less dazzled by the sheer size of compensation packages and numbers.

And companies successful in the world of tomorrow should rethink the design of their pay schemes, and how they communicate it to the financial community. How strong is the link between pay and performance in your company?

WHAT SHAREHOLDERS SHOULD DEFINE

- Clearly defined long-term minimal return on the market value of the investment
- Define the portion of value creation to be shared with executive management
- Define the portion of value creation to be shared with other employees
- Ask for a reconciliation between actual pay and the share of value creation

Shareholder rights under Swiss corporate law

So far, Swiss listed companies have not been confronted with much shareholder activism. At the shareholders' meeting of most Swiss listed companies resolutions are regularly approved by more than 90%. Nevertheless, Swiss shareholders do have rights they are increasingly willing to assert.

Jakob Höhn, Partner, Pestalozzi Lachenal Patry, Attorneys at Law, Zurich, Geneva, Brussels

Only very few shareholders make really use of their shareholders' rights despite the fact that Swiss corporate law provides a number of shareholders' rights:

- A shareholder may speak at the shareholders' meeting and bring motions related to the business to be transacted. E.g., if directors are up for election, any shareholder can propose other candidates.
- At the shareholders' meeting, a shareholder may request information about the business of the company from the board and the auditors. The board or the auditors must provide the information requested except in cases where they can show that it is important that the information be kept confidential.
- Any shareholder may propose at the shareholders' meeting that the shareholders resolve that certain matters shall be investigated by a special auditor.
- A shareholder may challenge a shareholders' resolution in court arguing that the resolution breaches provisions of the law or the articles. If the resolution needs to be registered with the commercial register, any shareholder can simply notify the office of commercial register and require that the registration be blocked.
- A shareholder may bring a liability suit against directors, officers or, in some cases even majority shareholders and argue that they have breached their duties.
- Shareholders holding shares with a total nominal value of CHF 1 million (or even a lower amount in many listed companies) may request that a business item be put on the agenda of the shareholders' meeting.
- Shareholders holding 10% of the share capital or shares with a total nominal value of CHF 2 million (or even a lower amount in some listed companies) may request that a shareholders' meeting be called and certain business discussed and resolved.
- Shareholders holding 10% of the share capital may request the court to appoint a special auditor to investigate certain matters of the company.
- Shareholders holding 10% of the share capital may request that the court order

the dissolution of the company or other appropriate measures. They must show to the court that they have important reasons for their request (e.g. continuous unequal treatment by the board).

Reasons for low shareholder activism in Switzerland

If shareholders use the above remedies, they can put significant pressure on the board and the management of a company. So, why do shareholders not make more use of their rights and put more pressure on Swiss listed companies? To the writer's knowledge, there are no studies in Switzerland to answer this question. However, it is likely that the following reasons have helped to keep shareholders' activism at a low level:

- Perhaps shareholders are not so unhappy with their board and management as one would assume when seeing all the media attention certain topics such as top executive remuneration are getting.
- The exercise of shareholders' rights is not for free. Active shareholders have to spend their own time and their own money, but the benefit goes to all of them. Therefore, for most shareholders it is easier to sell their shares if they are dissatisfied than exercising their rights.
- It is very difficult for shareholders to coordinate their actions with other shareholders. Shareholders have no access to the shareholders' register and, thus, do not know the addresses of the other shareholders.
- Up to now, it is generally believed that the existing shareholders' rights are not very effective. While this is not really true, it is still the prevalent view and few shareholders bother to consider to exercise their rights.

Because of this situation, there exist several initiatives to improve shareholders' rights. A revision of Swiss corporate law shall bring more effective information rights for shareholders, lower thresholds for the exercise of certain rights, improvement of the action to request the repayment of undue payments and separate elections of directors. However, these amendments of the law will not come into force before 2010 and it may very well be that at that time, shareholders will have become more active and simply will make more use of the rights to which they are already entitled today.

COMPANY PORTRAIT



IR Firm supports listed and financial services companies in the conceptualisation and implementation of their communications with the capital market participants. The company has extensive experience in developing and maintaining investor and media relations, in handling the communicative challenges of special situations (capital market transactions such as public offerings, rights issues and mergers & acquisitions) and in the conceptualisation and implementation of publications and IR websites.

The IR Firm advisory team expands this knowledge continually and creates added value for those companies which want to increase their profile in the financial community and to create a dialogue with their targeted audiences. In addition to traditional IR communications measures, IR Firm offers new instruments in the analysis of investors' perceptions and behaviour. The range of activities spans from advising on strategy regarding the conception and realisation of individual measures to regular measurements of results.

Building relationships with current and potential investors is primarily a matter of interface work. From a corporate standpoint, market opportunities, company strategy, management resources and company finances have to be brought into proper balance. In the capital market a constructive dialogue must be pursued with investors, financial analysts and financial journalists. Our in-depth experience and knowledge of how these interfaces function enhances the effectiveness and efficiency of our clients' investor relations activities.

IR Firm's specialists have experience in managing the complex interplay between companies and the financial community. Its client teams are headed by company partners and are individually set up for each specific project so as to best meet client needs. IR Firm also maintains a broad network of useful contacts with opinion leaders in research, education and practice.

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