



## Corporate Board Elections and Internal Controls



european corporate governance institute

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[Background to the Dialogue](#) | [Programme](#) | [Transcripts](#) | [List of attendees](#)



### Questions to Alexander Schaub

**Antonio Borges:** Thank you very much, Alex, for this very comprehensive review of everything that's happening in particular in Europe under the Commission's leadership in this field of corporate governance and for the main principles of dialogue that you defend. I'll make two quick remarks as you're thinking about the questions you may want to ask. Number one, this has been made very, very clear many times. Corporate control in Europe is exercised in a very different way. The problem of distance between shareholders and managers is not as clear when there are these block-holders but, of course, there is a very serious issue of discrimination across shareholders and minority investors losing in this conflict.

That's why the Commission's work is so important in enforcing transparency, disclosure, fighting market abuse and, in particular, focussing on related party transactions and therefore this concept of a powerful audit committee or the equivalent of an audit committee that will overlook the relationship across shareholders and possible discrimination against minorities becomes of crucial importance.

Number two, this idea of dialogue on convergence is very, very important even from a global efficiency point of view. There was a time when no large European company could neglect a listing in the US because otherwise they'd be operating at a very substantial handicap. Today it's the opposite. Many European companies are actually trying to withdraw from the US market because it has become too onerous and for reasons, which they don't quite understand, because it does not fit their own specific situations. So, we all end up losers in this objective of a global efficient capital market if we introduce additional barriers instead of converging towards something that fits the needs of everybody.

Now, let's move on to some debate. We don't have much time but I'd be happy to take a few questions and Alex will be ready to answer. Let's follow the usual rule of identifying yourselves.

**Question: Brian Chartier, Director Consultancy Services, Datacare Software Group:** Just a question or a comment maybe from yourself on the issue of dialogue and the need for dialogue and convergence because I totally agree with that. Do you envision a time where the dialogue will happen before the legislation? In other words, what we see today is different countries bring in the laws and then the talking happens after which is along the lines of, okay, they're here, how do we deal with it and how do we make it work. Will we come to a point where that dialogue happens before the legislation comes into play?

**Alexander Schaub:** This is exactly what we have to achieve and I'm, of course, aware that this is easier to say than to do. But if you take the example which Bill McDonough developed this morning, how are the two sides of the Atlantic able to handle the diverging rules on the auditing process which have been introduced in the US and in Europe, there we have done something which in the past has not been our habit. We knew that Sarbanes-Oxley would be implemented and we knew that in Europe we were about to launch the Eighth Company Law Directive on statutory audit, which I have mentioned in my presentation. Both are dealing with the same process. In the old world we would have let the two processes come to their end and then discovered that the rules on both sides somehow do not fit together. As American companies are listed in Europe and in the US and European companies vice versa, these companies would have been in the unfortunate and undesirable situation that either they comply with the rules on one side or the rules on the other side of the Atlantic or that they are trying to get delisted which in itself is not perhaps a positive thing. In any case, it's

extremely difficult, if not impossible, under the present circumstances. That is why we were looking for a solution and the classic solution for a real good bureaucrat – and I'm one of them – is, of course, to sit down and inquire about the possibility to negotiate an agreement. When I told this to Bill McDonough at the time, he said: "if you really need an agreement we can immediately stop our efforts because I have no power to negotiate an agreement and the SEC doesn't have one". They would need a law from Congress authorising them and that is a process, which you can immediately forget.

So, we were already at the end of our classic bureaucrat experience and at that stage we developed an idea, which is probably not in the classic arsenal. We decided that while both sides were preparing autonomously their draft legislation both sides would sit together regularly, compare notes and try to find out whether we were organising a nice beautiful major conflict again or whether these rules were fitting together in a way that we could exactly avoid in anticipation of such a conflict. And that is what happened. It was not in the headlines of the newspapers as a beautiful negotiation with drama and emotions would have been. It was a quiet process where the experts from Washington were coming to Brussels and the experts from Brussels were coming to Washington where they would compare how does this process develop under the draft rules on one side and can a company in the US wanting to work on both sides live under the two drafts developing in parallel? That led, of course, then to identifying a number of clear foreseeable conflicts and that led to a discussion how can we organise the process in a way that these conflicts are avoided. In this way McDonough and the PCAOB finalised their rules and we presented our proposal to Parliament and Council and as they are now drafted there is every chance that this will be a peaceful co-operation and that we can avoid conflict. In addition, what is in my view perhaps even more important, not only that in a practical given case we have in a preventive way avoided drama but what is much more important is the cultural experience of the teams on both sides which instead of, as traditionally, preparing war and talking about retaliation and other threats, both sides were sitting together and trying to find ways how to avoid the conflict.

Now, this is a case study where we have tried to illustrate how you can do it. I'm not naïve enough to say that this will now systematically work in all areas because it's clear that you need, to succeed in such an exercise, a certain culture on both sides. You need an openness, you need people who are ready to compare notes, people who are ready to respect that our world is very complicated and very different and things that are evident on our side are not at all evident on the US side and vice versa. But that if intelligent people are trying to find ways around this – and, by the way, are profiting from the comments from the other side – in order to improve the quality of the legislation, then we are making real progress. I can tell you from my experience in competition policy in the transatlantic co-operation, there's nothing more exciting and stimulating than common success in one potential conflict. This strengthens the determination of both sides to avoid other conflicts and stimulates the creativity and the imagination of people. I believe that is the way how we should progressively develop this co-operation in the transatlantic context but being understood that the transatlantic context is only one, of course, major chapter of co-operation in a global context. This experience should be reproduced, when necessary, with the Canadians, with the Japanese, with the Australians and with other major partners. The interesting thing is we have seen over the last two to three years that, for instance, the Chinese who are not yet at this stage of advance, it is quite striking the interest they have developed already now to start a regulatory dialogue with the European Union. Again, not because they would apply tomorrow these rules already but because their people – and they have top class intelligent people in their administration – have understood it is better to be involved in the process at an early stage and to understand the phases of development and to create a relationship of mutual trust and confidence.

So, I believe that despite all the complications – and there will be further dramas – we are on the right track and that there is a serious chance to reduce very considerably the risks of further accidents.

**Question: Andrew Clearfield, President, Investment Initiatives LLC:** During many discussions that I've had with the European Commission, your staffers, people like David Wright and Pierre Delsaux, one thing that they've always made clear to me is that, while they have been able to sound out fairly effectively the opinions of corporate issuers and bankers and some of the various other major interests in capital markets, it's been rather difficult for them to consult with overseas investors until and unless a comment letter goes out and they solicit general opinion on something which is more or less a *fait accompli*. One thing I've suggested to them – and I'd like to ask you about now, sir – is what would be the possibility of creating some kind of a more formal mechanism for sounding out major international investors, particularly American investors, who otherwise have no voice in the European Union, so that there'll be an ongoing dialogue between those investing in Europe and those trying to make European-wide rules and conciliate European rules with American rules?

**Alexander Schaub:** Well, in the philosophy I've tried to develop here, I don't see any particular obstacle to it as long as these investors are ready to co-operate in a not too heavy structure. Until this exercise here was started, there was not such a dialogue. Now it is quite well organised. It becomes, I believe, an annual event. There will be other countries perhaps being involved over time and if the international investors are not yet involved in this here, they could be involved either in this exercise or one can discuss about a specific structure. What is important is that we focus all our energy on preventive proactive ways of doing business instead of being totally absorbed with solving conflicts, which are still our burden from the past. All those who have had the pleasure and sometimes the displeasure to be involved in trade conflicts – and I've been in this business for a long time – will remember how frustrating it is to be dealing with decade-old conflicts dragging on and dragging on which stimulate confrontation and hostile emotions while what we are doing here is exactly the opposite. We are trying to anticipate where could the trains crash if nothing is done about it and what are the means to reorientate them into a different direction.

Now, I hasten to say this sounds much easier than it is in the real world because you need a certain type of mentality on both sides. You need the persons who are ready to do this and to seize this chance to get into a more constructive business and they are not always available, not always on our side, not always on our partners' side. So, you have to look for them and you have to try to develop practical cases, which are an incentive for others to work in the same way. I would pretend that what we are doing in the financial services on our side would not have been possible without the long and extremely constructive experience I have witnessed myself on the competition policy side. In competition we were also heading for dramatic confrontations where, at the times of Boeing/McDonald-Douglas and at the times of other major transatlantic merger projects which got into trouble and we were lucky enough at the time to find the right partners. One of them, by the way, is Joel Klein, who is now dealing with other difficult problems and I'm told is today as successful as he has been in conflict-avoiding in the competition area.

So, we have to consider this as a longer-term exercise and I believe that Europe has a certain competitive advantage in this business – and I'm not saying this is in a negative way. We have been for more than 40 years in this business of trying to avoid drama among the six and then 12, 15, 25 member states of the European Union. If you have 25 different legal systems and regulations, you are in danger every day that there is trouble and so we had to train our people every day how to avoid this. So, we are a kind of a living rapid action force who has learnt how to handle diverging rules and the possible conflicts with this. I found it always a bit amusing but probably not surprising that in the competition area, when we were in somewhat desperate situations, discussing with the Japanese and the Koreans and the broader world how can we handle that, that then our American friends came to see us and were saying how are you doing this in Europe in such a situation. You must have been familiarised with this. You must have seen such cases many times. What do you do in Europe? And I believe that there is a certain experience and culture accumulated over the years, a positive one – and there are certainly also negative ones and these have to be set aside. We have to focus on our positive constructive experience and see how we can share them with our global partners. That is the recipe we will try to follow.