



"Modernising Company Law and Enhancing Corporate Governance in the European Union – a Plan to Move Forward"

Communication from the Commission to the Council and the European Parliament
Brussels 21.5.03 COM (2003) 284 final

A Response by Traidcraft

SUMMARY

Traidcraft welcomes the consultation on the proposed action plan. In general we support the proposals put forward but in some areas consider that they need to be broadened and strengthened, particularly in the following two major areas:

i) Current provisions for stakeholder accountability are weak

Traidcraft welcomes the Communication's reference to third parties but we believe this lacks substance, especially in relation to the impacts of companies on third parties. As a signatory to international conventions the EU should be obliged to act in accordance with its commitments and in the interests of society. Companies are increasingly powerful and Company Law is a crucial means by which the EU can ensure that society is best protected from abuses of this power. The need for inclusion of social and environmental considerations is not set out in the Commission's action plan and this is a serious omission and a missed opportunity. In this regard the Communication does not appropriately modernise European company law and corporate governance. The reasons for the inclusion of social and environmental issues within company law are set out below.

ii) Provisions for shareholder accountability need to be strengthened

Traidcraft supports the Communication's intention to improve shareholder rights; but this should be delivered with a complementary set of actions to improve shareholder accountability. It is appropriate that corporate governance, which deals with the problem of separation and control of companies, should look at the issue of improving accountability for investment decision making. This is particularly important when the majority of companies are owned by individual members of Europe's voting public. To date there is poor accountability and communication about the impacts of investment decisions along the decision making chain. (This chain of impact for pension funds is as follows: individual pension fund holder – pension fund trustee – fund manager – investee company - individual members of the public impacted by company action.)

In addition the Communication is weak in two more minor areas. It assumes that board directors and auditors have the relevant competencies to undertake their roles. There is a competency gap in this field, which is particularly highlighted when companies view their risks. Fair Trade organisations have experience of balancing social and financial considerations in their corporate governance approaches and their operations. Without competent management certain crucial risks will be overlooked.

The Communication supports the 'comply or explain approach' to companies' compliance with corporate governance codes. Traidcraft agrees that compliance with codes needs to be monitored, but would urge the Commission not only to monitor whether codes are complied with but the content of associated disclosure. In the 'comply and explain approach' monitoring of the completeness of disclosure is frequently overlooked, even though its veracity and completeness is critical to the audience.

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A. TRAIDCRAFT

Traidcraft is one of the UK's leading fair trade organisations, selling food, household products, soft furnishings and clothing from nearly 100 producer groups based in 31 countries in Africa, Asia and Latin America. Traidcraft was established in 1979 and comprises two operational organisations: Traidcraft plc and Traidcraft Exchange, a registered charity.

Traidcraft plc is a medium-sized company which last year had a turnover of £12.06 million and made a profit of £416,000. Traidcraft plc has recently raised £3.25 million in a successful share issue.

Traidcraft Exchange is a development charity whose work spans capacity building amongst producers in developing countries, market access, policy development and advocacy. Through its Policy Unit, Traidcraft Exchange seeks to influence government policy and business practice in the North and the South to the benefit of the poor in the developing world.

Traidcraft is a pioneer of social accounting in the UK, having published the first independently audited plc report in 1993¹. Since then, the methodological approach (which Traidcraft developed initially with the New Economics Foundation) has been adopted and adapted by many larger organisations. It has also helped shape the AA1000 standard operated by the Institute of Social and Ethical AccountAbility (ISEA).

Traidcraft initiated the Just Pensions² project to highlight international development risks pertinent to investment and to capitalise on recently introduced UK regulation that Pension Fund's Statement of Investment Principles should disclose whether they consider social, environmental or ethical aspects.

A case study of Traidcraft plc and the replicability of its management and governance to an 'Average plc' is also attached.

¹ For the most recent Social Accounts, see www.traidcraft.co.uk

² www.justpensions.org

B. FAIR TRADE AND CORPORATE GOVERNANCE

The internationally agreed definition of Fair Trade is as follows:

“Fair Trade is a trading partnership, based on dialogue, transparency and respect that seeks greater equity in international trade. It contributes to sustainable development by offering better trading conditions to, and securing the rights of, marginalised producers and workers – especially in the South.

“Fair Trade organisations (backed by consumers) are engaged actively in supporting producers, awareness raising and in campaigning for changes in the rules and practice of conventional international trade.”³

Fair Trade is a growing in market size and impact. There are more than 800,000 small-scale producers working in nearly 3,000 grassroots organisations producing Fair Trade goods. In 2002, European Fair Trade Association members had a combined turnover of almost € 150m⁴. World-wide Fair Trade sales are more than half a billion Euros⁵. In 2002 sales of Fair Trade labelled products increased 22% on the previous year⁶ and this is estimated to have generated 50 million US\$/€ of additional income to producers and workers.

In these ways Fair Trade is contributing to the realisation of the Millennium Development Goals, which seek to reduce the number of people living in absolute poverty by half by 2015. Through engagement with a worldwide network of producers and partner organisations who work with some of the world's poorest communities the Fair Trade movement has first-hand knowledge of the conditions under which trade can be a powerful force for sustainable economic and social development. Company Law also has a role to play in promoting accountable and equitable trading relationships.

Fair Trade experience provides models of corporate governance for modernising company law. Fair Trade organisations take a pro-active approach to socially responsible business practices, focusing on the positive benefits of sustainable business practices for all. The success of Fair Trade in coupling profitability and economic effectiveness with international development objectives makes it a particularly valuable model to improve the corporate governance of mainstream businesses so that they have a better impact.

- Fair Trade organisations across Europe have experience of understanding their social impact so that they can manage their impacts for social benefit.
- Fair Trade organisations embed stakeholder engagement with their management approaches. This process enables the joint identification of risks to optimum business performance and enables appropriate action to be taken
- Fair trade organisations have corporate governance systems and management approaches which embed the balancing of social and commercial considerations. In particular Fair Trade organisations have expertise in balancing social and financial objectives and in managing global supply chains.

³ Source: FINE, formed through the informal co-operation between Fairtrade Labelling Organizations International (FLO), the International Federation for Alternative Trade (IFAT), Network of European World Shops (NEWS), and the European Fair Trade Association (EFTA).

⁴ Source: European Fair Trade Association (EFTA) www.eftafairtrade.org. Figure on the basis of retail-figure calculations

⁵ Graham Young for the King Baudouin Foundation (May 2003) 'Fair trade's influential past and the challenges of its future.' Where a billion equals a thousand million.

⁶ Source: Fairtrade Labelling Organizations International (FLO) www.fairtrade.net

C. COMMENTS ON MODERNISING COMPANY LAW AND ENHANCING CORPORATE GOVERNANCE IN THE EUROPEAN UNION – A PLAN TO MOVE FORWARD

Traidcraft welcomes the EU's plan to improve corporate governance approaches across Europe. In particular Traidcraft, as a social enterprise, supports the assertion in the Introduction (p3) that 'well managed companies, with strong corporate governance records and sensitive social and environmental performance, outperform their competitors. Europe needs more of them' Improved social and environmental performance by EU companies is certainly needed. There is a need in Europe not only to enhance corporate governance in general, but also of the governance of a company's social and environmental impacts. The Communication does not adequately address this aspect of company's impact as it only focuses on shareholders. Traidcraft encourages the EU to strengthen and broaden the areas of focus for corporate governance.

Our response sets out reasons why corporate governance of EU companies needs to be improved, followed by making specific comments and recommendations in relation to the different sections of the report.

Reasons corporate governance needs to address environmental and social issues

i) For the public good

The European Union, as the custodian of European society's well-being, is under an obligation to act in the interests of society. Companies are such an important and influential part of the public's everyday life; thus the regulation of companies is an important way in which the EU can ensure that society is best protected from harmful corporate impacts.

ii) To ensure compliance with international standards and goals

The EU - as a signatory to a wide range of internationally recognised conventions and initiatives on human rights and labour standards - should ensure that European companies adhere to these standards, both in the EU and through their influences overseas. Some European companies not only have poor social and environmental impacts, many do not respect international standards (to which the EU is a signatory) and have poor human rights records, use abusive purchasing practices⁷⁸ as well as degrade the environment. The following examples are a selection of European companies' problematic practices overseas.

- The UK's BP's investment in PetroChina made BP complicit in abusing human rights in Chinese occupied Tibet⁹
- Germany's Neumann Kaffee caused the eviction subsistence farming families from 60,000 hectares without consultation or compensation in Uganda¹⁰
- Italy's Parmalat's operations in Brazil were evaluated against ILO conventions by Brazil's Social Observatory in July 2001 and found the following:
 - Unjustified pressure to work weekends and holidays

⁷ Department of Trade and Industry press release P/2000/674 (10 October 2000) 'Byers Publishes Competition Commission Report On Supermarkets.' The report follows the decision by the Director General of Fair Trading (DGFT) in April 1999 to refer the industry. The Secretary of State has accepted the Commission's recommendations. The Commission has identified three situations where competition is distorted and operates against the public interest. The first concerns the relationship between supermarket chains and their suppliers including farmers. The Commission recommends that a Code of Practice should be established which would put relations between supermarkets and their suppliers on a clearer and more predictable basis. Stephen Byers said, "I agree that a Code of Practice should be introduced. Like the Commission I do not believe that a voluntary code would be adequate. The relevant supermarkets will have to give legally binding undertakings to comply with the remedies. I am asking the DGFT to approach those supermarket chains with 8% or more of the market (currently ASDA, Safeway, Sainsbury, Somerfield and Tesco) to agree a Code of Practice which would meet the concerns identified by the Competition Commission. This would include provisions for independent dispute resolution.

⁸ http://www.corporatewatch.org.uk/pages/whats_wrong_suprmkts2.htm#encouraging (August 2003) 'What's Wrong with Supermarkets?' The UK Competition Commission Report on Supermarkets (2000) cited 52 ways in which supermarkets exploit their dominant power over suppliers. At the heart of this is the supermarkets' refusal to enter into binding contractual agreements, leaving their suppliers without redress. Other practices include delaying payments by 15 days more than terms agreed; changing quality standards agreed without adequate notice; requiring buyback of unsold goods and making deductions from returns to cover wastage.

⁹ Free Tibet Press Release, (18 April 2002) 'Chinese soldiers' applaud BP's support for exploitation of Tibet while chairman stonewalls Tibetans at company AGM'

¹⁰ ActionAid UK (June 2003) 'Unlimited companies'

- Gender discrimination
- Persecution of union members¹¹
- The UK-listed British American Tobacco (BAT) continues to operate in Burma despite massive human rights abuses associated with the oppressive regime.

International standards apply globally. The EU needs to improve European companies' respect for and adherence to the core labour standards¹² of the International Labour Organisation and the UN's Universal Declaration of Human Rights. The latter has recently been set out for businesses in the 'U.N. Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with regard to Human Rights'¹³ and the European Commission would do well to promote these. Good corporate governance and the inclusion of accountability of social and environmental impacts within company law is crucial if the EU's part in globalisation is to contribute to sustainable development.

iii) To re-orientate companies to contribute solutions

The EU is not able to deliver some of its strategies and policies (e.g. on sustainable development, protection of human rights or poverty reduction) without the co-operation of business. The opportunity for business to play a positive role in driving sustainable development has previously been acknowledged by the Commission in the Communication on Corporate Social Responsibility. It is therefore appropriate that future action to improve corporate governance and company law should give companies a steer to consider environmental and social issues.

iv) To rebuild confidence in companies: to recognise responsibility is proportionate to impact and influence

There is a need to rebuild society's confidence in companies and their shares by making companies more transparent and accountable for their operations especially where they have a significant influence on communities overseas. Traidcraft's view is that where a company has influence or impact it has a proportionate responsibility and that Company Law should acknowledge this responsibility by promoting accountability to those impacted by a company. Some companies have significant adverse impacts on the environment and on society as a whole. To ignore these impacts would not only be irresponsible and morally wrong, it will also harm the long-term interests of business.

v) Legislative requirements of companies are needed

The democratically elected European Parliament in their response to the Communication on Corporate Social Responsibility believed that legislative changes would be required to improve business's impact on society and the environment. The areas of the UK's Business in the Community's Corporate Responsibility Index¹⁴ where companies score highest are in the areas where there is legislation.

Consequences of not addressing environmental and social impacts of companies in the EU's action plan

There are various consequences of leaving the action plan as proposed:

- The corporate governance of European companies will continue to give little recognition to the importance of transparency and accountability to different stakeholders
- Investors, consumers, suppliers and civil society will not be satisfied that companies have been directed to identify and assess their significant environmental and social impacts and - importantly - have the competence to manage their impacts in these areas. In particular, this is likely to lead to companies not assessing important issues such as: how bribery and corruption¹⁵ and labour standards impact on their business and their supply chain. A lack of guidance from the EU means that companies will pay insufficient attention to environmental and social issues such that poor

¹¹ Social Observatory, Brazil (2001) 'Social And Labour Programs And Conditions - Parmalat'

¹² ILO Declaration on Fundamental Principles and Rights at Work states that all countries have an obligation to respect, promote, and realise particular fundamental principles and rights i.e. freedom of association and the effective recognition of the right to collective bargaining; elimination of all forms of forced or compulsory labour; effective abolition of child labour; and elimination of discrimination in respect of employment and occupation

¹³ Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights, U.N. Doc. E/CN.4/Sub.2/2003/12/Rev.2 (2003). <http://www1.umn.edu/humanrts/links/norms-Aug2003.html>

¹⁴ Corporate Responsibility Index published (12/03/03) http://www.bitc.org.uk/news/news_directory/indexresults2002.html

¹⁵ For more details see www.publishwhatyoupay.org and www.transparency.org

practices continue, meaning that 'reputational' accidents such as Shell's experience with the Ogoni people are in fact actively in construction.

Actions in EU nations already undertaken to improve corporate governance of social and environmental impacts

Whilst companies have a legal responsibility to consider their shareholders this does not mean Company Law cannot evolve to take into account other stakeholders including the environment and local communities. This has been recognised in the increase in companies now reporting on their social and environmental impacts and has been reflected across Europe.

France has introduced recent legislative changes that require companies to report on their environmental and social impacts. Similarly in the UK the government's consultation on Company Law broadens significantly those areas a company needs to consider both as director's duties and in the proposed Operating and Financial Review.

C.1 Comments on The Communication's Key policy Objectives

The Communication sets out two key policy objectives that should be met by this area of Company Law:

- strengthening shareholders' rights and third parties' protection
- fostering the efficiency and competitiveness of businesses

Shareholders

Shareholders have responsibilities, which go with their rights. Shareholders have infrequently exercised their responsibility in both directions of their accountability. The largest shareholders are institutional shareholders – backed by monthly pension fund contributions, regular savings and insurance premiums. They have rarely consulted their contributing members (whose money they are investing) as to what sort of a future they would like to live in and then invested in accordance with their members' wishes. Traidcraft found through its work on Just Pensions that there is a poor chain of accountability and communications from pension fund holder to pension fund trustee to fund manager on the environmental and social impacts of investment. Likewise shareholders have frequently not exercised their responsibility in improving the governance of the companies they are invested in. It is only in 2003 that UK shareholders voted in significant numbers, for example voting against GlaxoSmithKline's remuneration package for its Chief Executive. The way in which investments are made has significant impact on companies' management strategies, plans and impacts. Traidcraft therefore calls on the EU to stimulate greater accountability in the investment decision making chain. Since corporate governance systems are designed to deal with the problems that result from separation of ownership and control of a company it is appropriate to consider the accountability of shareholders in the EU's company law and corporate governance action plan.

Third Parties

Traidcraft agrees with the following statement in the Communication on p8 - 'Ensuring effective and proportionate protection of shareholders and third parties must be at the core of any company law policy.' However whilst the Communication's reference to third parties is welcome it is too narrow in definition, focusing only on the need to protect shareholders and creditors. If the EU intends to work towards its Lisbon commitments, Sustainable Development commitments and the Millennium Development Goals for poverty reduction, a wider definition of third parties is needed.

C.2 Comments on Communication's EU Action Plan

RESPONSE TO SECTION 3.1.1 CORPORATE GOVERNANCE DISCLOSURE

Annual Corporate Governance Statement

Exchange of best practices within 40 or so corporate governance codes is welcomed particularly where such codes promote consideration for a company's social and environmental impacts.

The Commission states that it is not aiming for total harmonisation but to implement a few essential principles and rules. The Communication sets out the following for inclusion in an annual corporate governance statement made by listed companies:

- a) the operation of the shareholder meeting and its key powers, and the description of shareholder rights and how they can be exercised;
- b) the composition and operation of the board and its committees;
- c) the shareholders holding major holdings, and their voting and control rights as well as key agreements;
- d) the other direct and indirect relationships between these major shareholders and the company;
- e) any material transactions with other related parties;
- f) the existence and nature of a risk management system;
- g) and a reference to a code on corporate governance, designated for use at national level, with which the company complies or in relation to which it explains deviations.

Traidcraft supports the publication of an annual corporate governance statement as set out above and would make the following comments and additions.

Add to b) Explicit disclosure is needed to require the annual corporate governance statement to report the competencies of the board directors and committee members based on their training and experience. Investors, like all stakeholders of a company are interested in the ability of company senior management to identify risks accurately and manage them. There is a lack of skill on many boards in understanding social and environmental impacts of companies.

Convictions of board directors under national company law, as well as under civil and administrative law also need to be disclosed. This would motivate companies to abide by their nation's laws. Each offence is an indication of lax management which shareholders and potential investors need to know about.

Explicit reference to disclosure requirement proposed in Communication's section on director's remuneration:

- disclosure of the remuneration policy
- disclosure of details of remuneration of individual directors
- cost of directors share and share option schemes

Explicit reference needs to be made on the role and influence of non-executive directors especially with regard to appointing new members, remuneration, audit and corporate accountability/responsibility committees.

Add to f) It is not enough for a company to state the 'nature' of its risk management system. The corporate governance statement needs to state how risks are identified, prioritised and managed and the risk management system itself is reviewed.

Comment on f) The EU should also consider giving guidance on a good practice risk management system. This would make suggestions as to the process gone through to identify risks as well as alert companies to the breadth of skills needed within senior management to make a risk assessment; it would also emphasise stakeholder dialogue with diverse groups to correctly identify areas of risk. Engagement of companies with their stakeholders will enable companies to correctly identify areas where they are exposed and enable them to proactively

manage those risks. The EU could draw upon some of the thinking behind the UK's consultation document produced by the Operating and Financial Review working group on Materiality¹⁶.

Guidance will also need to include an explicit reference for companies to check that their impact and influence is not leading to violation of international standards or public policy objectives the EU has committed to (e.g. human rights, labour standards, sustainable development, poverty reduction).

The disclosure requirement needs to be phased in such a way that puts the onus on directors not to omit or misrepresent pertinent information. Ensuring that companies develop a rigorous risk management approach that is in tune with society's expectations will provide investors and stakeholders with adequate information to assess robustness of a company's corporate governance.

Review of compliance with various national corporate governance codes as well as whether companies risk management approach is correctly identifying key social impacts is needed. This will enable subsequent action can be undertaken to improve enforcement of these corporate governance elements. Such a review with subsequent action needs to be added to Medium term list of actions.

Information about the role played by institutional investors

Traidcraft fully supports the proposed obligation on institutional investors to:

- a) to disclose their investment policy and their policy with respect to the exercise of voting rights in companies in which they invest;
- b) to disclose to their beneficial holders at their request how these rights have been used in a particular case.

Traidcraft supports the disclosure of information by institutional investors since it should help to improve the chain of accountability for investment decisions. From the experience of different countries implementing different variations on the requirement on pension funds to disclose the inclusion of social, environmental or ethical issues in their statement of investment principles it is not sufficient to state disclosure of the policy. The Just Pensions project found that once pension fund trustees had developed a policy on social, environmental and ethical issues many did not change the management of the pension investments (either in-house or through an external fund manager) to reflect the changes in policy made.¹⁷ Traidcraft would propose the following underlined text as an addition to a).

Add to a) to disclose their investment policy and their policy with respect to the exercise of voting rights in companies in which they invest and how they manage the implementation of these policies;

Institutional investors should disclose their general approach to managing their investment policies which might set out how they review the performance of fund managers employed against their investment policy. This disclosure is required in addition to disclosure of specific action taken in a particular case.

This proposal should be brought forward from the medium term to the short term.

RESPONSE TO SECTION 3.1.3 MODERNISING BOARD OF DIRECTORS

Board Composition

Traidcraft welcomes the EU's increased emphasis on the role for non-executive directors. We agree that there is a need to limit the number of mandates any one director can hold if they are to properly undertake their governance role on the company boards they are part of.

¹⁶ 'The Operating and Financial Review Working Group on Materiality: A consultation document' (June 2003) Department for Trade and Industry, UK

¹⁷ Just Pensions (July 2002) 'Do UK Pension Funds Invest Responsibly?'

However, the term independent also needs to be carefully defined. Non-executive director's terms of appointment need to be restricted to ensure they remain independent and they should be prevented from sitting on the boards of the companies where there is a clear conflict of interest such as board of companies who are major suppliers or customers.

Company boards need to reflect the skills and expertise to face up to the challenges of the 21st century which go beyond short-term profits to the pressing global issues of climate change, population growth, poverty and diminishing natural resources. Companies need to be able to better manage conflicts with communities regarding control of resources and respect for human rights. At the moment most company boards do not have the breadth of competencies needed. Traidcraft welcomes the proposal that the company's risk management system is audited. However we are concerned that traditional audit companies do not have the skills to determine whether social and environmental risks have been properly identified and managed.

There is a missing discussion from the Communication on the balance between protection of public good and shareholders. There is a need for boards of directors to be accountable and liable should their company have any adverse impact on third parties. Accountability needs to be improved in three ways: through participatory forms of governance, in directors' duties and in stakeholders' rights. Traidcraft believes that directors' duties are fundamental to the proper running of a company. If directors are not given clear guidance on the issues they should consider, such as their significant environmental and social impacts, then it is likely that new areas for consideration will be ignored. In addition a right of redress is needed for stakeholders, particularly when local communities control over their natural resources is diminished by a company's action.

More democratic forms of participatory governance need to be explored to embed within the core of corporate governance considerations of social and environmental impact. Such considerations are not inimical to business success, as proved by the growth and success of fair trade companies. For example, the Day Chocolate Company¹⁸ is part owned by its raw material producers, representatives of whom sit on the Board. This is an example of an innovative corporate governance structure, which involves at Board level a stakeholder group that is significantly impacted on by the production activities of the company. This inclusion has in turn influenced Day Chocolate company's strategic decisions.

Directors' remuneration

Traidcraft agrees with the proposed four items relating to directors' remuneration. In addition Traidcraft would recommend that directors' remuneration be linked as a minimum to compliance with international standards as well as linked to positive social and environmental performance indicators.

Directors' responsibilities

Traidcraft welcomes the proposal that enables shareholders with certain percentage of the share capital to ask a court or administrative authority to authorise a special investigation into the affairs of the company. The threshold should not be set too high. The principle behind special investigation needs to be broadened and rightfully should also apply so that a third party (stakeholder) significantly impacted upon by the company has the right to initiate a special investigation. The ability to initiate special investigation needs to be brought forward from the medium term to the short term list of actions.

RESPONSE TO SECTION 3.1.4 CO-ORDINATING CORPORATE GOVERNANCE EFFORTS OF MEMBER STATES

Traidcraft agrees that a self-regulatory market approach with non-binding recommendations does not guarantee the adoption of sound corporate governance practices. Many codes of corporate governance suffer from poor enforcement, which tends to be largely focussed on whether a 'process' was followed or complied with rather than benchmarking corporate governance practices against actual reduction in liabilities and improvements in environmental and social performance.

¹⁸ www.divinechocolate.com

The 'comply or explain principle' only works when there is monitoring of the relevant corporate governance codes. The issue is not just whether member states monitor and enforce compliance and disclosure, but whether member states actually assess quality of the disclosure rather than just its existence. In the UK the Financial Services Authority sets out the initial listings requirements but has no role in checking the integrity or completeness of the disclosure. When the contents of an initial listing document is then questioned there is a vacuum as to who has the authority to force a change, to withdraw or to re-issue the listing.

Traidcraft welcomes the call by the Commission to establish some common EU wide rules and co-ordination of corporate governance codes. The Association of British Insurers whose members have a significant stake in the London Stock Market has produced useful guidance on the disclosure and management of social, environmental and ethical risks, which the Commission could usefully draw upon.

In order for the European Corporate Governance Forum to be credible to wider society, it must include permanent members who are qualified and experienced in the analysis of non-financial data.

RESPONSE TO SECTION 3.3 GROUPS AND PYRAMIDS

Parent and affiliated companies have a responsibility to third parties impacted by a company within the group or pyramid. Such a responsibility needs to be honoured especially when victims are in need of costly treatment caused by a company or when key household income earners are killed by a company either wilfully or through negligence.

RESPONSE TO SECTION 3.4 CORPORATE RESTRUCTURING AND MOBILITY

Traidcraft has a number of concerns with this section of the Communication. These relate to assumptions about mergers, considerations of whether corporate restructuring or the moving of company 'seat' or headquarters contributes to sustainable development and the transfer of accountability to third parties as a result of corporate restructuring.

Traidcraft is concerned at the Commission's implicit assumption in its discussion on facilitating cross-border mergers that increasing the size of companies is a good thing. As companies grow larger it becomes harder for senior management to have a proper understanding of their environmental and social impacts, which significantly compromises their ability to manage those impacts. It is easier for smaller and medium-sized companies to identify and manage their company impacts in a responsible manner.

Movement of 'seat' or Headquarters

It is not adequate for this Communication to state that social implications of moving the headquarters of a company from one country to another is covered in other Commission initiatives and to refer to the social partners work programme. Moving headquarters of a business not only impacts on the company's employees but also the knock-on relationships and activities of that company, particularly when a company is the main business in an area. Relocation will impact on its suppliers of products and services, both core and auxiliary (stationery, catering etc). The social benefits of social inclusion as a result of employment in supplier businesses may be greater than the actual numbers of those employed by the business which is considering moving its head quarters.

Enabling the frequent moving of a company's 'seat' does not contribute to sustainable development. If they are to contribute to sustainable development, businesses need to form partnering relationships. This is only possible when there is a degree of stability and predictability in the business strategy. Wider consideration of the knock effects on suppliers and whether a move of company headquarters will enhance a business's ability to contribute to sustainable development is needed in the EU's future actions in this area.

Corporate Restructuring

Traidcraft believes that the European institutions have a vital role in ensuring that European companies behave responsibly. We also believe that the EU's responsibility extends to European companies which have overseas subsidiaries or associated companies. Legislation should reflect a practice that the courts

have already accepted¹⁹, that parent companies cannot avoid liability for their overseas operations. Some companies have in the past avoided liabilities²⁰ through restructuring. Traidcraft believes that European Company Law should prevent companies from avoiding their liabilities through restructuring, merger or takeover.

In addition European law should be developed to ensure that, in the event of a merger or takeover, the offeree company is aware of the offeror companies' policies and practices on social, environmental and ethical issues. The offeror company should be required to disclose what changes (if any) it proposes on these policies. If there would be a significant dilution in policy and procedure, they should be required to explain why. The model provided by the UK's Transfer of Undertakings (Protection of Employment) Regulations 1981 (TUPE) would be a useful precedent in this context. It is also important that key policy differences particularly in the areas of social, ethical and environmental matters also need to be addressed prior to restructuring. Companies should not be allowed to drop or weaken policies in relation to their social and environmental performance without prior consultation with key stakeholders.

RESPONSE TO ANNEX 1 – LIST OF ACTIONS

Traidcraft supports the list of actions but recommends that some are strengthened and moved from the medium-term to the short-term list. In particular the following should be moved to the short-term list of actions and the underlined text indicates additional points associated with these actions.

- enhanced disclosure by institutional investors of their investment and voting policies and how they implement these policies (e.g. through evaluating the performance of fund managers employed.)
- Right for special investigation to be undertaken at the request of a shareholder or a third party significantly impacted upon by the company.
- Introduction of basic disclosure rules for all legal entities with limited liability.

¹⁹ See 'Corporate accountability in search of a treaty? Some insights from foreign direct liability' by Halina Ward, Briefing Paper No.4 (May 2002), The Royal Institute of International Affairs. This paper describes how the courts of England & Wales were satisfied that South African claimants had the right to bring their claims against UK or UK controlled entities, in the UK.

²⁰ In 1997 the Thor Group was restructured thereby putting the group's assets beyond the reach of litigants who had agreed a settlement with Thor. The Court of Appeal agreed that the demerger may well have been motivated by the desire to avoid payment of the agreed settlement and future claimants (*Sithole et al v. Thor Chemical Holdings Ltd et al*, 28 September 2000 at para 62).