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Shareholder Engagement in a New Environment and its Positive Impact on Corporate Governance in Germany

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by

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- 2 JAN 2003

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Abstract

Traditionally, activism by investors in Germany has not played a central part either in its corporate governance regime, or in Company Law doctrine. However, in the last years the role of shareholder engagement in Germany has changed considerably. As a response to developments in financial markets, society, technology and globalisation the legislator introduced a number of legal reforms in order to improve corporate governance. In this new concept the shareholders play a key role. However, currently shareholder rights in Germany are only exercised to a limited extent. This concerns private, corporate as well as institutional investors. To rely on a sound corporate governance system it is not only essential to have an appropriate legislation and a functional supervisory board, but also to have a healthy shareholder engagement[1].

Arguing that shareholder engagement has and will have an increasingly positive impact on corporate governance in Germany, this thesis aims to do three things. Firstly, it seeks to argue, normatively, that shareholder engagement does indeed matter, and can be beneficial for shareholders. Secondly it describes the current situation of shareholder engagement in Germany, while thirdly it provides proposals on how the current system could be reformed. Of course, "shareholder engagement" is a somewhat open ended term. To increase comprehension of the potential benefits of such engagement, as well as its current limits, this concept needs to be 'unpacked' and precise meaning given to it. In this thesis, I try to do that by developing, in chapter 1, what I call a "hierarchy of forms of shareholder engagement". The hierarchy arranges the forms of shareholder engagement according to their level of "aggression". This hierarchy is then used throughout the thesis to maintain a consistent analysis of the benefits of different forms of shareholder engagement, the extent of different forms, and the legal and practical changes I argue remain necessary to increase the effectiveness of these different forms of engagement.

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1 By shareholder engagement I mean the safeguarding of all justifiable interests, which are given to the shareholder by law or by the articles of association of the company.
In most of the literature the concept of "shareholder activism" is used instead of "shareholder engagement". I prefer to rely on the second wording. The reason being the fact that shareholder activism often has a negative connotation. Activists in connection with an annual general meeting are sometimes seen as troublemakers not only among the boards but also among investment managers. Moreover, activists also strive for popularity and attention. This is not the intention of shareholder engagement, which aims at positive results for the investors. The impression that legally protected activities by the shareholder are assessed as being negative should be avoided in this thesis. Additionally the concept of shareholder engagement in contrast to shareholder activism is more and more accepted in literature and market.
As the emphasis of this thesis is on the investment in securities of stock corporations, other forms of investment are only mentioned when appropriate (Partnerships, private limited companies, closed funds).

After the introduction (Chapter 1), the thesis is divided into three parts. Part A is the normative part; Part B the descriptive part; Part C provides suggestions to reform the system, including my own recommendation.

Chapter 2 of PART A provides the normative foundation of the thesis. In particular it shows that not only is shareholder engagement able to create shareholder value and other "intangible values" for investors, but also has an important function for a sound corporate governance system. A number of different surveys, which support this argument, are presented as well as some other surveys, which seem to go against my argument. In this respect the measurable and positive effect of the different forms of shareholder engagement is shown.

The descriptive PART B starts with Chapter 3. Here I introduce those instruments which support shareholder engagement. Explaining the role of the supervisory board in particular, but also the possibilities of proxy solicitation, helps to develop a good understanding of the environment of shareholder engagement.

Chapter 4 provides empirical evidence on the current practices and extent of shareholder engagement, whilst chapter 5 examines the non-legal environment for the exercise of shareholder engagement.

Chapter 6 turns to the legal environment for shareholder engagement, again applying the hierarchy of shareholder engagement developed in chapter 1.
Within this chapter I seek to demonstrate that the new liberties provided by Company Law are not yet applied appropriately, and that there is sufficient room for improvement.

In Chapter 7 I present the limits of engagement by investors, by explaining the shareholders' duty of loyalty towards fellow investors and the stock corporation.
PART C turns to the reform of the German corporate governance regime. It is divided into three chapters. To get a clear idea of what remains to be done in the future, it needs to be pointed out what has been achieved so far. More specifically, Chapter 8 focuses on the most recent activities of the legislator in the environment of shareholder engagement. Four important Acts and Bills are explained and assessed. Finally, an outlook into future legal initiatives is also provided.

In Chapter 9, I introduce a number of different authors who developed theories on how the legal environment could be reformed. The aim of those hypothesises is that shareholder engagement has to be pursued easily and has to benefit all stakeholders.

In Chapter 10 I provide my own suggestions and findings on the role of shareholder engagement. In particular I see three outstanding issues as central to improving shareholder engagement, namely: a) the financing of shareholder engagement; b) investors' reluctance and lack of awareness; and c) shortcomings in Company Law.
The suggestion on financing shareholder engagement requires pointing out, as it plays an important role in the overall concept. As a result I make a proposal on how the system existing so far could be reformed by using a working model called "agency without authority." According to this model the institutional investor could pass on the costs, which arise out of his engagement, to the issuer.
In this chapter I conclude that a mixed reform between an extension of the areas where investors could take influence, and a cut back of other rights is necessary so that shareholder engagement will act as a guarantor for sound corporate governance in Germany.

1. Chapter: Introduction

1.1. Defining the Position of Shareholder Engagement in the Corporate Governance System

1.1.1. The Pillars of German Corporate Governance

"One share – one vote"[2] is nowadays probably one of the most discussed principles within the Company Law in Germany. It provides a basic right in the concept of corporate governance, namely the influence shareholders could execute on corporate policy and decision making via the general meeting. According to the German Stock Corporation Act, shareholder rights include in particular the safeguarding of the assets; the right to be informed on company matters; participation in the general meeting; and protection- and control mechanisms through share- and voting quorums. Moreover, they also include the right of action against the issuer or a third party and more.[3]

Along with the supervisory board and the legislation, the general meeting is supposed to build a three pillar base for the regime of corporate governance.

Some jurisdictions preferred to install one board with executive and non-executive directors in it. In contrast to this, the two-tier control mechanism describes another way of corporate governance: The separation into a management and a supervisory board, which consists of shareholder and employee representatives.

A number of recent crises, such as those of Telekom, EM-TV, Mannesmann, DaimlerChrysler, Holzmann, Volkswagen[4] and others, have raised doubts as to whether this governance system is still suitable for a leading financial market place.

To strengthen the second and central pillar, the German legislator has increased efforts to reform the Stock Corporation Act of 1965 in the last years, with the aim of improving existing governance mechanisms and introducing new remedies.

One cornerstone of the new legal framework within Company Law was the work of the government panel on corporate governance[5] (May 2000 – July 2001). The task of this

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2 Regulated in § 134 AktG; albeit with a number of exceptions.

3 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.214

4 There are numerous articles in the web considering this topic. See, for example,

Hoffritz, Jutta „Rüstige Rentner dringend gesucht" in die Zeit 12/2000 at www.zeit.de/2000/12/200012_ar_kontrolle.html; Hamann, Götz/Hauch-Fleck, Marie-Luise/Uebel, Conny „Legitim, legal, illegal" in die Zeit 13/2001 at www.zeit.de/2001/13/wirtschaft/200113_bewertung.html; Kramarsch, Michael H. „Für die Vergütung von Managern werden Maßstäbe gesucht" in Frankfurter Allgemeine Zeitung 08/09/01 Wirtschaft

5 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf or press report 304/01

panel was to scrutinise the German Stock Corporation Act and to find ways through which it could be improved by national and international corporate governance standards. In particular they described the legislator's task as follows:

> "Due to the institutionalisation and internationalisation of shareholdings, the globalisation of the capital markets, and the rapid development of information technologies, the German corporate law system was placed under increasing pressure to adapt to the ever changing requirements of the market[6]".

The central proposal of the panel was that the Federal Government is to appoint a group of experts to draft and continuously improve a Code of Corporate Governance[7]. Although the Code is not legally binding for stock corporations, they are advised to document it in their articles of association. The reason for this is that they have to comply with it or explain their opting out (§ 161 AktG) in the Bundesanzeiger (Federal Gazette). Moreover, the panel also proposed the creation of a legal framework for this new, flexible instrument. Consequently, a number of findings by the panel resulted in the TransPuG of 2002. Surprisingly, the rights of investors in Germany can be seen as the most advanced within Euroland[8]. Although it would be wrong to overrate this view, it does at least indicate that German legislation is competitive compared to that of other financial markets.

Technical and social developments were also taken into account by the legislator. Examples include the possibility to vote the stocks electronically, the (unfortunately) short-lived fashion to change bearer share equities into registered shares, and the increased importance of the stock market not only for the pension scheme but also as an attractive investment for individuals.

Historically, the general meeting as the third pillar of corporate governance has not played a decisive part in the German corporate governance system, although the capital presence might indicate the opposite. This derived from the still dominant position of the custodian banks and their reluctance to interfere with corporate policy and decision making. However, over the last years the financial, social and political environment has changed and with it the role of the shareholder meeting. By acknowledging that it needs to become a load-bearing pillar in the concept of corporate governance, the shareholder meeting experienced an increase in value. It is slowly becoming a body which, within its limits, exercises control over the company. Therefore shareholder engagement is decisive for influencing the general meeting.

While the two-tier board and the new Code, respectively Company Law, have become accepted load-bearing pillars in the German corporate governance system, the general

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6 Report of the Government Panel on Corporate Governance July 2001 to download on "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf or press report 304/01

7 German Corporate Governance Code to download at www.corporate-governance-code.de/eng/download/DCG_K_E200305.pdf (Last alteration: 2.6.2005)

8 Kramarsch, Michael H. „Für die Vergütung von Managern werden Maßstäbe gesucht" in Frankfurter Allgemeine Zeitung 08/09/01 Wirtschaft

meeting still falls back because of underdeveloped shareholder engagement. The big issue here remains the widespread lack of awareness of shareholder rights and its accompanying responsibility, or more directly, investors' ignorance. This becomes obvious when looking at the capital presence at general meetings in Germany[9], and the uncritical approach towards governance issues[10].

However, due to the debate on the performance of certain corporations' board members; recent legislator's reforms on the Stock Corporation Act; and enhanced investor relations management, shareholder engagement is gaining in importance to market participants.

1.1.2. The Position of Shareholder Engagement in Corporate Germany

In a study carried out by the fund corporation, DWS, on corporate governance[11] German companies do not meet the standards of international investors[12]. While the legislation has been found shareholder friendly, the quality of the supervisory boards was assessed as being poor[13]. Moreover, the commitment to shareholder-value, achieved by the teamwork of the executive board, the supervisory board and the shareholders, is largely viewed as inadequate[14]. This statement is reinforced when considering the failure of corporate governance in certain German stock corporations like EMTV, Comroad, Kabel New Media and others.

Although these reforms have not yet made the German system comparable with the Anglo-American scheme[15], the introduction of the German Corporate Governance Code[16] implied considerable progress in this area. Even if the code is a recommendation rather than a statute, it indicates the fact that governance is up-valued in Corporate Germany. This positive development will most probably improve the value of German corporations to a significant extent[17] as the capital markets will acknowledge enhanced transparency and publicity.

Due to Corporate Germany's ignorance on such matters, foreign institutional investors as well as the legislator have led the push for German companies to adopt corporate

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9 See Figure 6: Presence at DAX 30 AGMs (1998-2005)

10 Although critique could get quite loud, the majorities in a number of general meetings do not reflect this. Good example: Especially institutional investors and shareholder associations criticised severely the management of DaimlerChrysler before the 2004 AGM. Nevertheless, the activities of the board were approved by 88% of the votes.

11 Hetzer, Jonas/Papendick, Ulrich „Unter Freunden" in Manager Magazin 8/01, 31. Jahrgang at p.92-98

12 Hetzer, Jonas/Papendick, Ulrich „Unter Freunden" in Manager Magazin 8/01, 31. Jahrgang at p.94

13 Hetzer, Jonas/Papendick, Ulrich „Unter Freunden" in Manager Magazin 8/01, 31. Jahrgang at p.97

14 Hetzer, Jonas/Papendick, Ulrich „Unter Freunden" in Manager Magazin 8/01, 31. Jahrgang at p.97

15 Hanloser, Stefan „Proxy-Voting, Remote-Voting und Online-HV: § 134 s.3 AktG nach dem NaStraG" in Neue Zeitschrift für Gesellschaftsrecht (NZG), Volume 8, 27.04.2001 p.355-358 at p.356

16 German Corporate Governance Code to download at www.corporate-governance-code.de/eng/download/DCG_K_E200305.pdf (Last alteration: 2.6.2005)

17 California Public Employees' Retirement System "Why Corporate Governance Today?" A Policy Statement - to download at http://www.calpers-governance.org/principles/domestic/why/page01.asp August 14, 1995, Especially the pension funds and shareholder associations represent this opinion

governance standards. Some companies' resistance to these changes can still be observed in, for example, the lack of transparency of the managements' remuneration.

1.1.3. The Position of Shareholder Engagement in a Global Context

Shareholder engagement has also become more important as a result of increased internationalisation of the investors. Companies tend to acquire capital from around the globe, while investors hold more and more cross-border shares. Considering the merging of capital markets, it can be predicted that the trend to international investments will increase, because the introduction of the Euro is harmonising the European stock market[18]. Also the increasing popularity of shares as a means of payment with takeovers and mergers of corporations will speed up the globalisation of capital markets.

In contrast to globalisation effects, it appears that shareholder rights do not cross the border. Although the legislation protects the rights of any investor, they are currently rarely exercised by foreign shareholders. For institutional investors, as opposed to private shareholders, this is about to change due to new technical developments, increased legal requirements, and possibly the realisation that corporate governance matters.

Now it is more important than ever to exercise the possibilities, which are given by Company Law. Still the question remains if the conditions, which are set by the legislator and corporations, are sufficient to revalue the global shareholder as a supporter of the corporate governance system.

The European Union has taken on the challenge of harmonising the different systems of corporate governance by putting this topic into its programme of action[19]. In a first step they had formed a panel on a Modern Framework for Company Law in Europe, the so-called "Winter-Committee"[20]. The findings of this panel lead to the recognition within the EU-Commission that improving the rights of shareholders of companies across the Member States was a priority[21]. The result is an Action Plan on modernising Company Law and enhancing corporate governance in the European Union. Especially, within

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18 Baums, Theodor/Schmitz, Rainer „Shareholder Voting in Germany" Paper No. 76, 1998 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm

19 Hommelhoff, Peter „Die OECD-Principles on Corporate Governance - ihre Chancen und Risiken aus dem Blickwinkel der deutschen corporate governance-Bewegung" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR), Vol. 30, No.2, March 2001 at p.238-267 at p.262

20 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" 2002 to download at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf

21 European Commission - Directorate General Internal Market „Company Law & Corporate Governance" 2006, to download at http://europa.eu.int/comm/internal_market/company/shareholders/index_en.htm

this context, an up-valuation of shareholder rights with a global alignment could be expected within 2006[22].

To avoid the so-called "Delaware Syndrome" or "race to the bottom"[23], the harmonisation of each member state's Company Law is essential[24]. This means that a member state should not refrain from important Company Law standards in order to win incorporation against another member state. Important considerations are tax issues, corporate control and labour market requirements.

The European Union is seen to have less developed shareholder rights than the US[25]. The willingness of the EU-Commission to improve the legal framework in this area is consequently necessary to keep the European financial services market competitive.

In summary, corporate governance in Germany and in the European Union still varies between the member states to an unsatisfactory extent. Hence, the role of the individual or institutional investor and the funds has to be upgraded. While the legislator has recognised, to a degree, that good shareholder engagement indicates additional support in the corporate governance system, German companies only slowly accept that an active shareholder is not only a guarantor for stability, but is also a marketing tool in gaining new investors.

1.2. The Hierarchy of Forms of Shareholder Engagement

Before explaining the environment of shareholder engagement, an escalating hierarchy should be drawn. This will support a better understanding, help to clarify an assessment and make the consideration of the environment for shareholder engagement easier not only with regard to its benefits but also to its costs.

The hierarchy of shareholder engagement helps to define an easy and promising approach for the shareholder to request information or address his concerns towards the management in a reasonable manner. The hierarchy of shareholder engagement can also help the management of listed companies to better understand and react to the requests and concerns of the investor. Consequently the suggested hierarchy serves both parties.

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22 European Commission - Directorate General Internal Market " Corporate governance: Commission proposals to make it easier for shareholders to exercise their rights within the EU" 2006, Reference: IP/06/10, to download at http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/06/10&format=HTML&aged=0&language=EN&guiLanguage=en

23 Tuerks, Robin A. "Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.74 - In the beginning of the 20th century a competition was held between the different US-States for the laxest Company Law. Winner was the state of Delaware, which was in 1915 considered the most liberal state to incorporate.

24 Lo, Benjamin T. „Improving Corporate Governance: Lessons from the European Community" Indiana University School of Law 1994 to download at http://www.law.indiana.edu/glsj/vol1/lo.html; more detailed: Stith, Clark D. "A "race to the bottom" in the European Community" in Federalism and Company Law 1991from p. 1549 at p. 1581

25 Report to the European Commission by Delphi International LTD in Association with Ecologic GmbH "The Role Of Financial Institutions in Achieving Sustainable Development" 1997 to download at www.europa.eu.int//comm/environment/finserv/fitotal.pdf

The following possibilities, ordered according to the level of "aggression" against the company that they entail, can be identified and distinguished:

1. Requests for Information

Requesting information from the issuer helps the shareholder improve his assessment abilities of the company's situation and thus of his investments.
This information might be provided by the company in form of the annual report or the general meeting agenda or more general via their webpage. Alternatively, the shareholder also has the right to request more specific information directly from the company.
As he receives the information directly from the company there is no fractional loss and 100% accuracy can be expected. The information request is a practical and easy tool for the investor and should serve to build the basis for further shareholder engagement. The costs for pursuing this right are insignificant.

2. Shareholder Negotiations

Shareholder negotiations are not regulated and should therefore be considered as the least "aggressive" form of shareholder engagement. The company is not obliged to enter negotiations with its investors.
Seeking dialogue with management is an elegant way to tell those that are responsible that they need to do better or make certain changes to corporate practice. If these measures fail the shareholder could still consider taking his issues to a higher level. Negotiations should be used by the larger shareholding investors in the company.
The costs of talks are high as they need to be well prepared and should be carried out by members of senior management (when pursued by an institutional investor). In any case the chances of success need to be scrutinised prior to entering into discussions with the company.

3. Speaking at the General Meeting

Speaking at the general meeting is closely related to the request of information. This right provides the shareholder with the possibility to address and formulate critical issues towards a large group of shareholders and the management. Being asked a question, management needs to react and provide either a sufficient answer or the requested information. The costs for this right are insignificant. However, a positive or negative impact on the reputation needs to be considered.

4. Shareholder Proposal or Calling in a General Meeting

The next step the shareholder could consider is making a proposal to the general meeting. Although proposals by shareholders are very rarely successful, not only are

they an effective tool to force management to take a stand, but also to bring the raised issues closer to other shareholders.
A shareholder proposal is emphasised when it is accompanied by a proxy fight. Additionally, providing the shareholder fulfils the legal requirements set out in Company Law he is also entitled to call a general meeting to discuss urgent issues.
This option requires careful consideration as it is likely to have an impact on the company's reputation. The costs for a shareholder proposal or calling a general meeting are low.

5. Using the Voting Right

This tool primarily serves the purpose to show management either that it is doing a good job by voting for its recommendations; or to indicate that it requires improvement by voting against. This latter option is a vote of no-confidence, which, providing the opposition casts sufficient votes, puts a considerable strain on the board.
The vote should be withheld when the shareholder believes that he is not sufficiently informed over an item on the agenda, but believes that there is an issue. Unfortunately, because of the low attendance at German general meetings, withholding the vote rather indicates passivity than an active analysis of the issues within the company.
The shareholders' approval becomes necessary for a number of corporate decisions being brought about. This is particularly important with regard to resolutions on dividend payments; mergers and acquisitions; composition of the supervisory board, or altering the statutes. Even when the investor uses a proxy the costs for using this form of engagement are low to medium.

6. Legal Actions

Legal actions are often seen as a "last resort" for the shareholder, sometimes correctly. Not only because they carry a financial risk for the plaintiff, but also because they might hinder the economic or social development of the company. Typically, they serve either to recover financial losses (which could be attributed to at least negligent behaviour of the management) or to maintain the status of the investor. Due to the impact a legal action might have, management is well advised to take this form of engagement seriously and to take appropriate measures. Taking a certain action will probably have a negative impact on the reputation of the investor. In addition to that the costs in relation to the risk could be assessed as high.

7. Exit as a Form of Shareholder Engagement?

Simply selling the shares is still a very powerful and popular tool to express dissatisfaction with corporate performance. Although it constitutes a form of shareholder activity, I shall argue that it does not constitute a form of shareholder engagement as defined for this Thesis. More particularly, "exit" is designed for the

expressed purpose of breaking with the company, not to engage with it. Certainly the effect of selling shares may well reduce the share price and force management to change their policies. However, this is not the motive of those who sell their shares. Therefore I shall treat a sale, or "exit", as a last resort of shareholder engagement. Also known as "voting with the feet", this measure does not harmonise with the notion of corporate governance. With the exception of custodian fees and possible Capital Gain Tax, exit costs are insignificant.

Part A - Normative Part

2. Chapter: Why Shareholder Engagement in Germany Is Beneficial

Shareholder engagement does matter and is becoming more and more relevant for corporate Germany and investors themselves[26]. The Deutsche Börse bid for the London Stock Exchange in early 2005 revealed the increased influence of shareholders on corporate decision making in quite a dramatic way. In this case the shareholders of the Deutsche Börse (77% Anglo-American investors) evaluated the takeover offer for the London Stock Exchange as far too expensive. Management of the Deutsche Börse did not consult its own shareholders prior to the bid, yet a number of shareholders succeeded in demanding an end to the takeover battle. The CEO and the chairman of the supervisory board wore the consequence and resigned.

The question answered in this chapter is whether shareholder engagement is beneficial both for shareholders and for stakeholders under certain conditions. I shall begin by examining whether engagement is advantageous for corporate performance and hence, shareholder value. To recognise a potential positive impact of shareholder engagement on the stock price (material), a number of different tests will be applied below. These tests are also important to determine which forms of activity (hierarchy of shareholder engagement) deliver most value. Additionally, it will also be investigated whether shareholder engagement has an impact beyond the financial performance of the company (intangible). Therefore, the effect on the company's social responsibility will also be illuminated.

Having addressed shareholder value we then turn to the stakeholders' interest. Here the question will be asked whether there is a cause of friction between shareholder engagement and the stakeholders' interest.

Finally, it is also necessary to evaluate negative impacts of shareholder engagement on corporate Germany.

2.1. The Nexus of Interests

Jensen and Meckling[27] see the nexus of interests and relations among the stakeholders of a company as follows: They state that,

> "if (a) the firm is viewed as a nexus of complete contracts with creditors, employees, clients, suppliers, third and other relevant parties, (b) only contracts with shareholders are open-ended; that is, only shareholders have a claim on residual returns after all other contractual obligations

26 In contrast to Germany shareholder engagement in Anglo-American countries is considerably further developed. Due to legal requirements and client pressure institutional shareholders in the UK or the US are more likely to engage themselves in the company they are invested in than their continental European counterparts.

27 JensenMichael/Meckling, William "Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure" in Journal of Financial Economics 3 1976 p. 305-360 at p. 312

have been met, and (c) there are no agency problems, then maximisation of (residual) shareholder value is tantamount to economic efficiency."

Under this scenario, corporate governance rules should be designed to protect and promote the interests of shareholders exclusively.

As it has just been argued, in order to understand the complexity of shareholder engagement it is important to get an overview of the different interests of investors and the interests of *different* investors. Although this latter group will be scrutinised in detail in Chapter 4.1., at this point it needs to be pointed out that shareholders could be categorized as institutional, corporate, private, state, foundational or associational. Hence, an accumulation of different interests is a logic consequence.

For instance, looking at the role of pension funds requires a unique approach. Pension funds pursue a long-term profit maximisation, as any other policy would be contradicting their investors' interests. In contrast, other shareholders have different expectations from shareholder engagement. The manager of a Hedge Fund is certainly more interested in the short-term influence of shareholder activism on the equity price, while the manager of a Social Responsibility Fund[28] requires that certain intangible standards be fulfilled.

2.2. Shareholder Engagement and its Influence on the Equity Price

At this point, the crucial question shall be illuminated whether action taken by the investor could improve the financial well-being of shareholders. As it can be seen in Figure 28 (appendices), the instruments to measure this effect are not as manifold as the detected results. A number of different authors tried to measure the influence of activism with the help of different characteristic features. Unfortunately, the costs of engagement were rarely part of the studies. However, the results varied considerably, depending on the scope of the investigation. The same is valid for other approaches like making an inquiry among fund managers, or looking at the difference between the prices of ordinary shares compared with those of preference shares. Due to these heavy deviations of the empirical data, a critical approach is appropriate and the conclusions need to be reflected in the whole context.

Deriving from the thesis that shareholder engagement serves good corporate governance and thus has a positive effect on the performance of the company, it needs to be investigated whether this impact results in a higher equity price. By using the hierarchical approach, it will be explained that different forms of engagement have different effects on the share price.

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28 E.g. Companies like Ethos, SAM - Sustainable Asset Management in Switzerland or Funds like Sarasin Sustainable Eco, DWS Invest Sustainability Leaders or BHF Sustain Select

Here it is important to point out that there is no direct or indirect empirical evidence to prove any value-enhancing effects of information requests and speaking at the general meeting. Furthermore, it is vital to keep in mind that the focus of this thesis is primarily on Germany.

2.2.1. Corporate Governance Rating

Measuring the impact of shareholder engagement is difficult. Therefore, it is beneficial to support the argument that shareholder engagement matters by taking into account the value of good governance in general as well. One good tool in this respect is considering ratings. They are informative - and they give us a hint of what value might attach to shareholder engagement - but no more than that. Ratings primarily serve to avoid risks when picking stock, and therefore only have an indirect connection with the claimed hierarchy. However, corporate governance ratings also scrutinize some aspects of shareholder engagement. For instance the option to call a special meeting; the response to shareholder proposals; and vote requirements or shareholder approval of option plans[29] are among the tested variables.

In 2002, Institutional Shareholder Services introduced their Corporate Governance Quotient (CGQ) for the US stock market. This product is a rating system that rates stock corporations according to their corporate governance performance. The source data, which contains up to 61 variables, is derived from public disclosure documents, press releases and corporate websites, and is then verified by analysts and stored in a database. Issuers can access a webpage, giving them the ability to make changes to their corporate governance rating if they believe that something has been stated wrongly or if improvements to the company's corporate governance system have been made. This tool enabled fund managers to choose stocks considering the corporate governance performance of a company and consequently, to avoid the sorts of scandals that beset Enron, Worldcom, Ahold and Parmalat.

In September 2003, ISS extended this corporate governance rating to 3.000 stock corporations in the MSCI EAFE index (Europe, Asia, Far East, Australia) and the MSCI World index.

Figure 1: Corporate Governance Rating by Countries[30]

Country	Average CGQ		Country	Average CGQ
United Kingdom	90,3		Japan	42,5
Ireland	86,1		Netherlands	41,4
Australia	73,2		Hong Kong	39,5
New Zealand	66,3		Italy	38,7

29Global corporate governance rating criteria of Institutional Shareholder Services 2006 to download at http://www.issproxy.com/institutional/analytics/globalcgqcriteria.jsp

30 Average Corporate Governance Quotient - Source: Institutional Shareholder Services Oct 2004

Switzerland	61,2		Denmark	34,2
Singapore	59,4		Spain	33,6
France	57,4		Sweden	22,8
Finland	57,3		Belgium	19,7
Austria	56,2		Greece	19,0
Canada	51,6		Norway	14,7
Germany	45,4		Portugal	10,9

In a study carried out by Lawrence Brown on "The Correlation between Corporate Governance and Company Performance"[31], which was based on the Corporate Governance Rating by ISS, Brown found that companies in the bottom decile of industry-adjusted CGQ by ISS have five-year returns that are 3.95% below the industry average, while firms in the top decile of industry-adjusted CGQ have five-year returns that are 7.91% above the industry-adjusted average[32]. Hence, the difference in performance between the over- and underperformers is 11.86%.
For the advocates of good corporate governance this is certainly proof that governance matters. However, this result only provides a positive result to the extent that fostering shareholder engagement rules has a positive impact on the stock price.

2.2.2. The Willingness of the Shareholder to Spend more for a Company with an Active Corporate Governance

The willingness of investors to spend more on shares of a company with good corporate governance is of limited meaning with regard to the value of shareholder engagement. Assessing shareholder engagement with this instrument does not deliver very sound conclusions, as this approach does not give evidence of the engagement itself and hence lacks reliability. However, it is at least an indicator that corporate policy is of some importance to the shareholder.
According to an international study carried out by McKinsey & Company in 2000[33], investors were prepared to pay 18% to 27%[34] more for shares providing they adopt a functioning corporate governance system. Interestingly, in this study three-quarters of the investors say that board practices are at least as important to them as financial performance when evaluating companies for investment. In Latin America, almost half the respondents consider board practices more important than financial performance[35].

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31 Brown, Lawrence "The Correlation between Corporate Governance and Company Performance" Georgia State University, 2004 to download at http://www.issproxy.com/pdf/Corporate%20Governance%20Study%201.04.pdf

32 Brown, Lawrence "The Correlation between Corporate Governance and Company Performance" Georgia State University, 2004 to download at http://www.issproxy.com/pdf/Corporate%20Governance%20Study%201.04.pdf

33 McKinsey & Company "Investor Opinion Survey on Corporate Governance" Research Paper June 2000

34 Interestingly investors in Europe and Northern America were less prepared to spend more on well-governed companies compared to their Asian or Latin American counterparts. Stated in McKinsey & Company "Investor Opinion Survey on Corporate Governance" Research Paper June 2000 at p.16

35 McKinsey & Company "Investor Opinion Survey on Corporate Governance" Research Paper June 2000 at p.1

This indicates that shareholders considerably rely on other corporate governance pillars that are not engagement related and even prefer stability before shareholder value.
Certainly, this statement also relies on the fact that a corporation, which is active in practising corporate governance, does not have anything to hide. Providing that a company offers maximum transparency, it can easily be concluded that it is healthy. Therefore, the willingness to accept a higher price for the share is concomitant with the perfect flow of information between the company and the investor[36]. Although the assumption that investors intend to spend more on shares of a company with good corporate governance, is a useful indicator, it should not be overestimated, as probably other considerations influence it and moreover, it is only based on a subjective view.

2.2.3. Shareholder Negotiations

Shareholder negotiations are a fundamental part of the engagement hierarchy. Their positive impact compared to shareholder proposals (which will be explained in detail in the following chapter) is remarkable[37]. One reason for this might be the fact that some shareholders perceive proposals more as door openers, forcing management into negotiations. On the surface, it is difficult to see a difference between the two approaches, as both intend to achieve a goal defined by the shareholder. Hence, it could be assumed that shareholders believe that a negotiated agreement, aiming at a reciprocal approach, results in performance improvement; compared to a proposal, which emphasises a deplorable state of affairs within the company and reveals a disagreement between investor and management. Monks points out that real shareholder victory lies not in toppling ineffective CEOs, but in creating an environment of revitalisation making these upheavals unnecessary[38]. The argument might be valid that shareholder proposals can distract managers and harm their abilities to manage effectively, while a negotiated agreement considers the managements' points of view.
The great difference between proposal and negotiation is the chosen approach. While the first is drastic and attracts attention, the latter is considerably smoother and inconspicuous (in the end it might even be difficult to determine which party prevailed over the other).

Considering all this, one may conclude that investors prefer cooperation instead of confrontation. To use the words of Monks again:

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36 Compare with: Pellens, Bernhard/Hillebrandt, Franca/Ulmer, Björn "Umsetzung von Corporate-Governance-Richtlinien in der Praxis" in Der Betriebs-Berater (BB) Volume 56 No.24 14.06.01 p.1243-1250 at p.1243

37 See Figure 28: Studies Showing the Correlation between Equity Performance and Corporate Governance Activity

38 Monks, Robert A.G. "Relationship Investing" Columbia University, 1993 to download at www.ragm.com/archpub/ragm/relationship_investing.html at p. 11

> "This is certainly a step forward as shareholders are not there to tell corporations how to run their business; they should be there to tell corporations that they need to do better"[39].

Understandably, the accomplishment of shareholder negotiations is closely related to the targeted issue. It could be assumed that in those consultations stakeholder issues are playing a more important role than proposals. Successful initiatives by employee shareholders for example to raise the share of disabled employees; to accept new environmental standards or to alter takeover defences, can have different effects on the development of the stock price if they are negotiated with the influence of stakeholder issues rather than pure shareholder proposals.

However, one great weakness of studies showing a positive effect of shareholder negotiations on the stock price is that they concentrate on the Anglo-American judicial system. There the management decides the degree to which it will comply, while in Germany (§ 119f AktG) and a number of other European countries (e.g. France), the successful shareholder resolution is binding. Just as it is the case with shareholder proposals, these studies should be considered carefully when coming from a Continental-European angle. Not only the differing judicial systems but also other influences need to be taken into account, such as stakeholders or whether the objections by management are qualified. This means that most of the empirical data cannot simply be applied to another environment.

2.2.4. Shareholder Proposals

As it will be described later in this thesis, shareholder proposals are a fundamental part of the shareholder engagement concept.
Conclusions and results of studies investigating shareholder proposals are as numerous as the studies[40] themselves. While a majority of studies show a positive effect, some even show a negative (respectively neutral) correlation between shareholder proposals and stock price performance. At first this seems to be astonishing. However, it should be kept in mind that shareholder engagement sets in when the company's performance

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39 Monks, Robert A.G. "Relationship Investing" Columbia University, 1993 to download at www.ragm.com/archpub/ragm/relationship_investing.html at p. 12

40 See Figure 27: Studies Showing the Correlation between Equity Performance and Corporate Governance Activity; Karpoff, Jonathan M./Malatesta, Paul H./ Walkling, Ralph A. "Corporate Governance and Shareholder Initiatives: Empirical Evidence" in Journal of Financial Economics 42, 1996 at p.365-395; Gillian, Stuart L./ Starks, Laura T. "Corporate Governance Proposals and Shareholder Activism: the Role of Institutional Investors" in Journal of Financial Economics 57, 2000 at p.275-305; Smith, Michael P. "Shareholder Activism by Institutional Investors: Evidence from CalPERS" in The Journal of Finance Vol. 51 No.1 March 1996 at p.227-252; Nesbitt, Stephen L. "Long-Term Rewards from Shareholder Activism: A Study of the "CalPERS Effect"" in Journal of Applied Corporate Finance, Winter 1994 at p.75-80 and "The "CalPERS Effect" on Targeted Company Share Prices" January 26, 2001 to download at http://www.calpers-governance.org/alert/selection/WilshireRpt.pdf; Strickland, Deon/ Wiles, Kenneth W./Zenner, Marc "A Requiem for the USA - Is Small Shareholder Monitoring Effective?" Journal of Financial Economics 40, 1996 at p.319-338; Bizjak, John M./Marquette, Christopher J. "Are Shareholder Proposals All Bark and No Bite? Evidence from Shareholder Resolutions to Rescind Poison Pills" in Journal of Financial and Quantitative Analysis Vol. 33, No.4 December 1998 at p.499-521, Gompers, Paul A./Ishii, Joy L./Metrick, Andrew "Corporate Governance and Equity Prices" July 2001 to download at http://icf.som.yale.edu/Conference-Papers/Fall2001/gov.pdf

is perceptibly below average. How is it possible that a proposal aiming at an improvement has no, or even negative, effect? One reason is seen in misdirected activism[41]. It was found that the types of board and compensation reforms advocated by proposal sponsors have not been found to be value-enhancing corporate governance devices[42].

Interestingly, the list of applicants shows that the initiator of the proposals could be ascribed to any camp of shareholders[43]. As the conclusions of the studies are closely dependent on the way shareholder engagement was exercised, it is advisable to make a distinction between the studies showing a positive, negative or insignificant effect.

Certainly, a number of proposals (e.g. confidential voting) do not target a better performance at all. Others are primarily aiming at certain provisions within the articles of association (takeover defence, board reform) and might display its purpose only in certain cases (takeover, crisis of the board). Therefore, a better distinction of the proposals is necessary to recognise a possible positive effect. Moreover, it seems to be suitable to include individual company characteristics such as structure of ownership or size. For example, a poison pill[44] is unattractive for smaller investors, but considerably attractive to majority shareholders.

Moreover, the vast majority of results are based on studies carried out in the US. This makes it difficult to transfer them to other financial markets like the German market. A different legislation, pension scheme or development of the market will probably falsify the findings to a certain extent. For instance in Germany takeover preventing provisions are relatively unknown (and unnecessary) due to the *shareholder structure* of most German companies, which hinders any hostile approach. Here it is the remuneration of the board that is the target of active investors, rather than the statutes or provisions of the company. Therefore, the target of shareholder proposals is not applicable for a number of regimes. The expressiveness of most studies remains limited, but it certainly explains the incredible high interest in new case related investigations.

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41 Romano, Roberta "Less is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance" in Yale Journal on Regulation Volume 18, 2001 p.1-78 at p.7

42 Romano, Roberta "Less is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance" in Yale Journal on Regulation Volume 18, 2001 p.1-78 at p.18; Hetzer, Jonas/Papendick, Ulrich „Unter Freunden" in Manager Magazin 8/01, 31. Jahrgang at p.94

43 Romano, Roberta "Less is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance" in Yale Journal on Regulation Volume 18, 2001 p.1-78 at p.15; also compare with Pozen, Robert " Institutional Investors: The Reluctant Activists" in Harvard Business Review Jan 1994 p.140-149 from p.140ff

44 Definition taken from Gompers, Paul A./Ishii, Joy L./Metrick, Andrew "Corporate Governance and Equity Prices" July 2001 at http://icf.som.yale.edu/Conference-Papers/Fall2001/gov.pdf p.37-42:

Poison pills - These securities provide their holders with special rights in the case of a triggering event such as a hostile takeover bid. If a deal is approved by the board of directors, the poison pill can be revoked, but if the deal is not approved and the bidder proceeds, the pill is triggered. In this case, typical poison pills give the holders of the target's stock other than the bidder the right to purchase stock in the target or the bidder's company at a steep discount, making the target unattractive or diluting the acquirer's voting power. The early adopters of poison pills also called them "shareholder rights" plans, ostensibly since they give current shareholders the "rights" to buy additional shares, but more likely as an attempt to influence public perceptions. A raider-shareholder might disagree with this nomenclature.

2.2.4.1. *Studies Showing a Positive Relation between Corporate Governance and Stock Price Performance*

The studies taken into account for this thesis were all investigating the effect of activism (almost exclusively shareholder proposals) of a certain group of investors in a certain area, over a certain period of time. (An overview and summary of the studies is provided in Figure 28).

A highly celebrated study was that of Gompers, Ishii, and Metrick in which the authors calculated that an 8.9 percentage point difference between 1990 and 1998 in firm value was partially "caused" by each additional governance provision[45]. They created a Governance Index for a certain number of companies based on 24 governance provisions (ranging from golden and silver parachutes, to poison pills and special meeting requirements[46]) and studied the relationship between this index and several forward-looking performance measures. The result of this study was a comprehensible relation between corporate governance and the share price. Taking into account the higher agency costs with companies, which have more governance provisions, this finding is even more upvalued[47].

Although this study does prove the connection between governance provisions and a higher equity price, it relies too much on aspects that should protect the company from takeover, and ignores other features of corporate governance. Hence, an idea is given about a number of cost intensive provisions upheld by the company to maintain control, but necessary factors of corporate governance are omitted. Especially shareholder engagement features like enhanced investor relations or improved proxy voting, which are important for an informed and reasonable shareholder; deserve mentioning in connection with this matter. The reference to the expositions on the price difference between the ordinary share (with voting right) and the preference share (no voting right) - (Chapter 2.2.7.) already indicate that an analysis of certain shareholder engagement factors in this study would have been desirable. It also needs to be emphasised that shareholder engagement is mostly a higher cost factor for the company than agency costs related with certain governance provisions in the law or the statutes.

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45 Gompers, Paul A./Ishii, Joy L./Metrick, Andrew "Corporate Governance and Equity Prices" July 2001 at http://icf.som.yale.edu/Conference-Papers/Fall2001/gov.pdf p.36

46 Definitions taken from Gompers, Paul A./Ishii, Joy L./Metrick, Andrew "Corporate Governance and Equity Prices" July 2001 at http://icf.som.yale.edu/Conference-Papers/Fall2001/gov.pdf p.37-42:

Golden parachutes – These are severance agreements which provide cash and non-cash compensation to senior executives upon a triggering event such as termination, demotion, or resignation following a change in control. They do not require shareholder approval.

Silver parachutes – These are similar to golden parachutes in that they provide severance payments upon a change in corporate control, but unlike golden parachutes, a large number of a firm's employees are eligible for these benefits.

Special meeting requirements – These provisions either increase the level of shareholder support required to call a special meeting beyond that specified by state law or eliminate the ability to call one entirely.

47 Gompers, Paul A./Ishii, Joy L./Metrick, Andrew "Corporate Governance and Equity Prices" July 2001 at http://icf.som.yale.edu/Conference-Papers/Fall2001/gov.pdf p.34

Moreover, other corporate governance factors like special disclosure requirements or continued education of supervisory board members were also not taken into account. Consequently, it needs to be questioned whether the 8.9% are a realistic surcharge for companies with good corporate governance. Probably this figure needs to be put into perspective and thus only represents an approximate value.

Other studies which were carried out by Bizjak, Marquette[48] on the rescission of poison pills; by Strickland, Wiles, Zenner[49] on the effect of proposals, which were sponsored by the United Shareholders Association (USA); or by Nesbitt[50] who investigated the performance of proposals by California Public Employees' Retirement System (CalPERS)[51]; all showed a measurable positive effect of shareholder engagement on the stock price.

2.2.4.2. *Studies Showing a Negative or Neutral Relation between Corporate Governance and Stock Price Performance*

In contrast to the studies mentioned above, there are a number of authors who discovered a neutral or even negative effect on the stock price. For example, Gillan and Starks[52] detected a slight positive impact of proposals sponsored by active individual investors, but they also found a small but measurable negative impact of proposals of institutional investors. Unfortunately, they only focused on voting outcomes and short-term market reactions, which put the findings into perspective. Other studies like that of Karpoff, Malatesta, Walkling,[53] who conclude that the probability of receiving a shareholder corporate governance proposal is negatively related to a firm's market-to-book ratio, operating return on sales, and recent sales growth[54]; or Forjan[55] on the effect of shareholder proposals, found a neutral respectively negative return in connection with shareholder proposals. Again, the results of these studies have to be considered carefully. Both studies were carried out mainly in the Eighties and ended in the beginning of the Nineties. Assuming that the realisation that shareholder engagement

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48 Bizjak, John M./Marquette, Christopher J. "Are Shareholder Proposals All Bark and No Bite? Evidence from Shareholder Resolutions to Rescind Poison Pills" in Journal of Financial and Quantative Analysis Vol. 33, No.4 December 1998 at p.499-521

49 Strickland, Deon/ Wiles, Kenneth W./Zenner, Marc "A Requiem for the USA – Is Small Shareholder Monitoring Effective?" Journal of Financial Economics 40, 1996 at p.319-338

50 Nesbitt, Stephen L. "Long-Term Rewards from Shareholder Activism: A Study of the "CalPERS Effect"" in Journal of Applied Corporate Finance, Winter 1994 at p.75-80 and Nesbitt, Stephen L. "The "CalPERS Effect" on Targeted Company Share Prices" January 26, 2001 to download at www.calpers-governance.org/alert/selection/WilshireRpt.pdf

51 California Public Employees' Retirement System: http://www.calpers.com

52 Gillian, Stuart L./ Starks, Laura T. "Corporate Governance Proposals and Shareholder Activism: the Role of Institutional Investors" in Journal of Financial Economics 57, 2000 at p.275-305

53 Karpoff, Jonathan M./Malatesta, Paul H./ Walkling, Ralph A. "Corporate Governance and Shareholder Initatives: Empirical Evidence" in Journal of Financial Economics 42, 1996 at p.365-395

54 Karpoff, Jonathan M./Malatesta, Paul H./ Walkling, Ralph A. "Corporate Governance and Shareholder Initatives: Empirical Evidence" in Journal of Financial Economics 42, 1996 at p.392

55 Forjan, James "The Wealth Effects of Shareholder-Sponsored Proposal" in Review of Financial Economics 8, 1999 p.61-72

was necessary to support corporate governance was developed in the second half of the 1980's[56], it is not surprising that the first proposals were not destined to succeed economically.

2.2.4.3. Conclusions

As there is considerable variation in the results of these US-focused studies, it is crucial to determine the quality of the data and its interpretation when making an assessment. Taking this and all studies into account, an objective observer could cautiously conclude that shareholder proposals could indeed show a positive effect.
Although it has to be acknowledged that it is almost impossible to specify a value of shareholder proposals, the statements of Smith and Strickland/ Wiles/Zenner could be kept in mind, saying that in general shareholder engagement is worthwhile as the returns are far higher than the costs[57].
In Germany Drobetz, Schillhofer und Zimmermann[58] show a positive effect of differences for firm-specific corporate governance. Despite this finding it must be alleged that shareholder proposals in this country do not have the same effect compared to those in the US. This derives from the fact that proposals by other investors rarely succeed. To blame is the omnipotence of the banks, whose custodian voting rights almost certainly determine the results of the poll before it is carried out.
Therefore, Germany might serve as a good example for the assumption that shareholder negotiations are the more successful way of shareholder engagement than shareholder proposals.

2.2.5. The Value of the Voting Right

It is also possible to ascribe a value to the voting right, although it is not necessarily positive.

2.2.5.1. The Counterproductive Side of the Voting Right

A good example that the voting right could be counterproductive and destroy value is the Girmes case[59]. Here Girmes AG encountered financial troubles, which endangered the stakes the shareholders put in the company. The revitalisation plan by management,

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56 Romano, Roberta "Less is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance" Yale Law School and National Bureau of Economic Research; Draft: October 26, 2000 p.1-78 at p.3

57 Michael P. Smith "Shareholder Activism by Institutional Investors: Evidence from CalPERS" in The Journal of Finance Vol. 51 No.1 March 1996 at p.251 (return: $ 19 million - costs: $ 3.5 million); Deon Strickland, Kenneth W. Wiles, Marc Zenner "A Requiem for the USA – Is Small Shareholder Monitoring Effective?" Journal of Financial Economics 40, 1996 at p.335 (return: $ 1.3 billion - costs: 22.75 million)

58 Drobetz, Wolfgang/Schillhofer, Andreas/Zimmermann, Heinz „Corporate Governance and Expected Stock Returns: Evidence from Germany" Arbeitspapier No. 110, 2003 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html

59 Girmes Ruling: Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs - BGHZ Volume 129 at p.136

major shareholders and major creditors intended to waive outstanding claims and to set down the capital in a ratio of five to two. An active shareholder representative promoted that a reduction of the capital in the ratio of five to three would be sufficient. He succeeded with his plan in the general meeting, but failed to convince the creditors. The consequence was that the company became insolvent and was liquidated.
The Girmes case illustrates a negative example for shareholder engagement and shows, just like the following exposition, that the voting right needs to be exercised carefully and on an informed basis.

2.2.5.2. Takeover and Merger

As § 13 s.1 s.1 UmwG requires shareholder approval when the management decides to merge with or takeover another company; and investors could engage in corporate decision making by using their vote. This means that in a general meeting their voting decision is crucial for the coming about of a takeover or merger. Consequently, their vote will have a positive or negative impact on the material value of the company.

In 2002, the legislator introduced the WpÜG – "Wertpapiererwerbs- und Übernahmegesetz" (Security Acquisition and Takeover Act). Its aim is to provide guidelines for a fair and systematic bidding procedure, without fostering or preventing takeovers. Moreover, it should improve the flow of information to the affected shareholders (in order to make an informed voting decision) and employees in the case of a takeover, as well as safeguarding the legal position of minority shareholders[60]. This objective already indicates that the emphasis of this Act was more or less laid on a capital market approach. Valid reasons include that the attraction for shareholders in a takeover is the accompanying expectation that the stock price increases, as the "bid price" is usually considerably higher than the market price immediately before the bid. This anticipation derives primarily from synergy and efficiency effects of a takeover or a merger. Moreover, often the mismanagement of a company is also made out as a reason for a takeover bid. The replacement of management might be an indicator for an increase in the stock price.

These reasons form the basis for the predominantly positive acceptance among the investors. Surprisingly often enough this positive assessment is not based on facts. According to studies by Jansen/Körner[61] and Schneider/Burghard[62] this is not justified as only a minority of the hostile and friendly takeovers lead to a market value increase

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60 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Regelung von öffentlichen Angeboten zum Erwerb von Wertpapieren und von Unternehmensübernahmen" 2001 (BT-Drucksache 14/7034) to download at http://dip.bundestag.de/btd/14/070/1407034.pdf at p.28

61 Jansen, Stefan/Körner, Klaus "Fusionsmanagement in Deutschland" Witten 2000 to download at http://notesweb.uni-wh.de/wg/wiwi/wgwiwi.nsf/vwFiles/StudieFM/$FILE/Jansen+Fusionsmanagement+Abstract.pdf at p.28

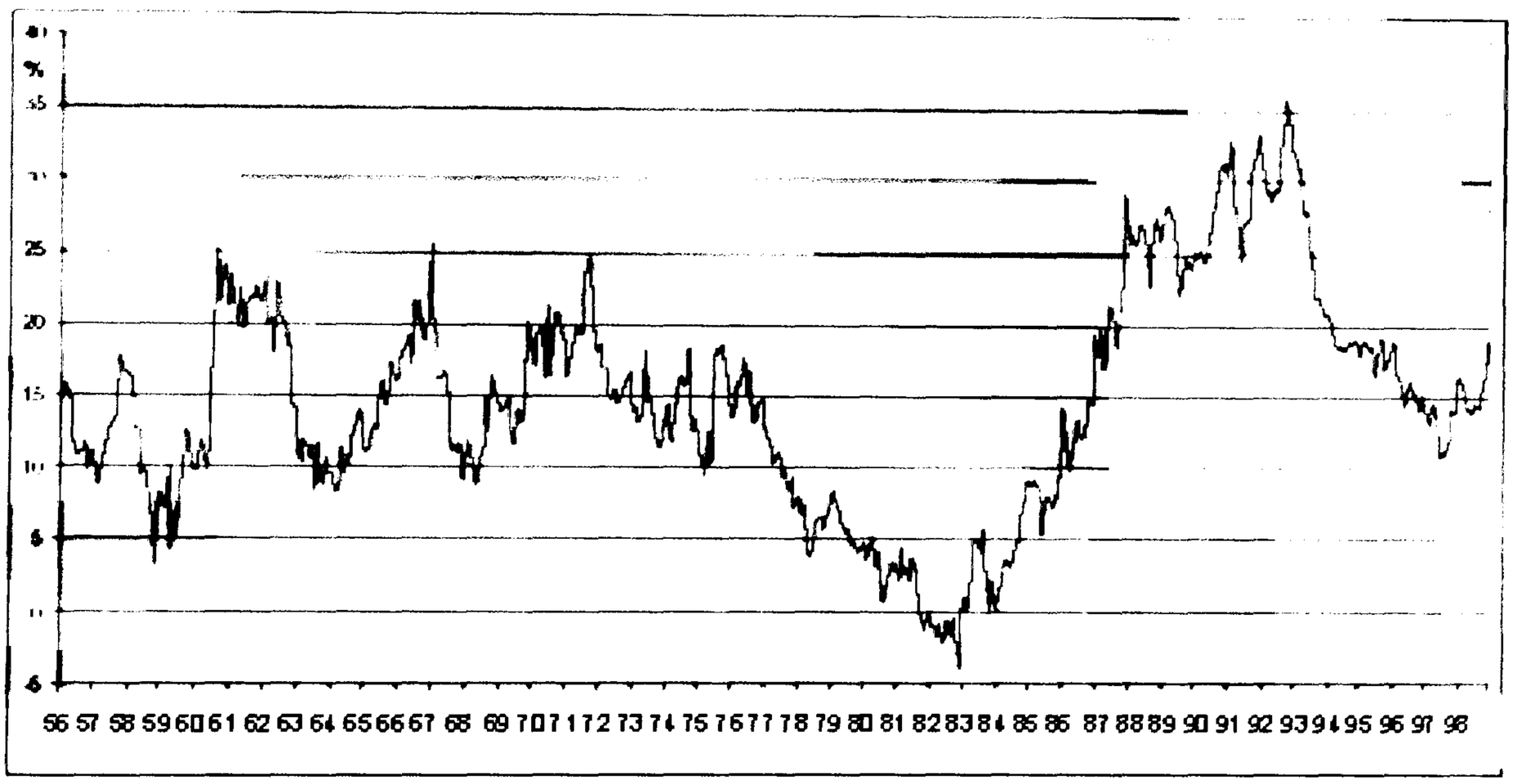
62 Schneider, Uwe/Burgard, Ulrich "Übernahmeangebote und Konzerngründung" in Der Betrieb (DB) 2001 p. 963-969 at p.964f

and thus to a better equity price. Consequently, as takeovers and mergers are often "value reducing" shareholder engagement becomes crucial for the plans of the management, as informed voting decisions need to be made.

2.2.5.3. *The Price of Ordinary Shares minus the Price of Preference Shares: Is it the Value of the Voting Right?*

Maybe the easiest way to determine the value of the voting right is simply to compare the quotation of ordinary shares and preference shares (Figure 2).
As preference shares do not have a voting right, it could be assumed that the surcharge for ordinary shares in the same stock corporation is the value of the voting right. However, due to the great difference between the spread in the stock price between those two types of shares[63] it is not possible to give a universally applicable statement for German companies.

Figure 2: Average Price Difference of Ordinary Shares compared to Preference Shares in Listed German Stock Corporations 1956-1998[64]



It is worthwhile to look at the average of 17% between 1956 and 1998[65]. As the price of ordinary shares is often considerably higher than that of preference shares despite the paid dividend being lower, it could be argued that the increase in value is dependent on the vote[66]. Generally speaking, this assumption is correct, but some explanations are required. The capital requirements of the different companies are certainly reflected in

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63 see chapter 5.3.3. Preference Shares

64 Daske, Stefan/Ehrhardt, Olaf „Der Kurs- und Renditeunterschied von Stamm- und Vorzugsaktien – eine Untersuchung am deutschen Kapitalmarkt" 2000 to download at www.fmpm.ch/files/4th/DaskeEhrhardt.pdf p.24

65 Daske, Stefan/Ehrhardt, Olaf „Der Kurs- und Renditeunterschied von Stamm- und Vorzugsaktien – eine Untersuchung am deutschen Kapitalmarkt" 2000 to download at www.fmpm.ch/files/4th/DaskeEhrhardt.pdf p.1

66 Grabert, Frank „Stimmrechtsvertretung im Aktienrecht – ökonomische Bedeutung und rechtliche Problematik" Dissertation with the University of Hohenheim to download at at http://ourworld.compuserve.com/homepages/mox/diplom.htm at 2.1.2

the spread. Surprisingly, it has been found that higher tax, which has a negative influence on the equity price of preference shares and its attractiveness for shareholders, could easily be ignored[67].

However, a measurable but not linear impact on the value of the voting right stems from the shareholder structure. Daske and Ehrhardt state that a high and low share of widely held stock (Streubesitzanteil), as well as a dominant position of a major investor prevent considerable changes within the shareholder structure and are, therefore, reducing the value of the votes[68]. Furthermore, Daske and Ehrhardt add that in contrast to this, the value of votes will be enhanced if the separation of cash-flow and vote enables a major shareholder to obtain the majority of the shares, with a relatively low capital share compared to the controlled asset[69]. These conclusions for the German stock market appear strange. This derives from the fact that ownership of German stock corporations is mostly concentrated and control-oriented[70] (e.g. interweaving, which results from crossholdings of blue-chip companies or large private shareholders, who control the majority of the votes). Consequently, the existing shareholder structure often prevents greater influence of minor investors in general meetings. However, this does not appear to explain the spread in the equity price between ordinary and preference shares. This fact is underlined by the relatively low capital presence in the general meetings[71].

Although the voting right is rarely used in general meetings in Germany, it is crucial for the coming about of a takeover. Consequently, the predator company is only interested in acquiring shares that carry a voting right. This results in a higher price at the stock exchange and could explain the pricing spread between preference shares and ordinary shares. However, regarding the attempts of hostile takeovers in which the number of votes was crucial, none in German corporate history was successful. Even the Mannesmann AG - Vodafone takeover battle in 2000 ended as a friendly takeover.

In context with shareholder engagement and equity price it is also necessary to state that alterations to the articles of association affecting the voting right result in markdowns[72]. Hence, individual corporate policy is also able to have an effect on the equity price.

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67 Daske, Stefan/Ehrhardt, Olaf „Der Kurs- und Renditeunterschied von Stamm- und Vorzugsaktien – eine Untersuchung am deutschen Kapitalmarkt" 2000, to download at www.fmpm.ch/files/4th/DaskeEhrhardt.pdf at p.29: This research found that higher taxation does influence the capital costs by only 0,21% annually

68 Daske, Stefan/Ehrhardt, Olaf „Der Kurs- und Renditeunterschied von Stamm- und Vorzugsaktien – eine Untersuchung am deutschen Kapitalmarkt" 2000, to download at www.fmpm.ch/files/4th/DaskeEhrhardt.pdf at p.33

69 Daske, Stefan/Ehrhardt, Olaf „Der Kurs- und Renditeunterschied von Stamm- und Vorzugsaktien – eine Untersuchung am deutschen Kapitalmarkt" 2000, to download at www.fmpm.ch/files/4th/DaskeEhrhardt.pdf at p.33

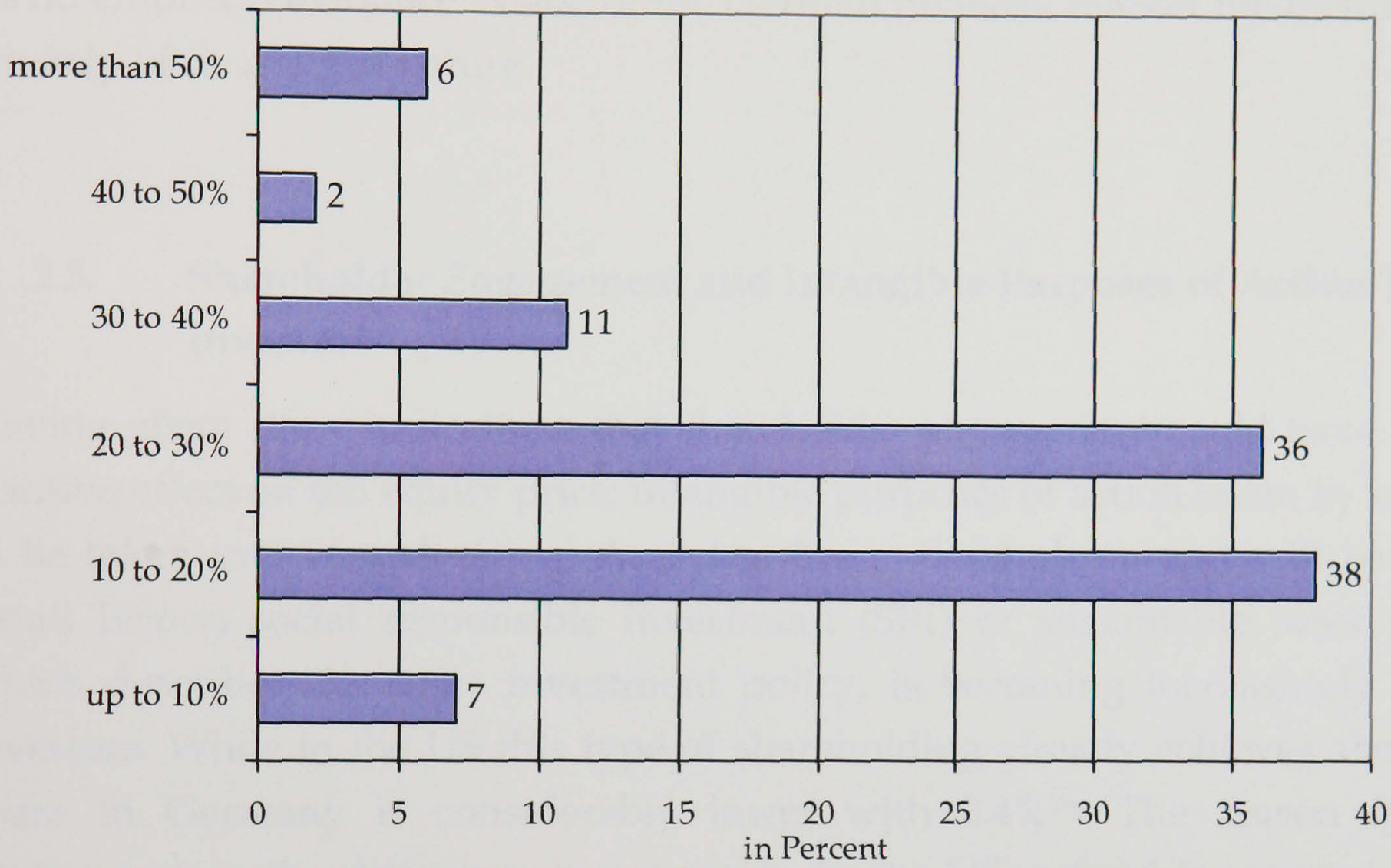
70 See Figure 29: Shareholder Structure of Selected Stock Corporations 2004

71 See Figure 6: Presence at DAX 30 AGMs (1998-2005)

72 Hahn, Dieter „Die feindliche Übernahme von Aktiengesellschaften: Eine juristisch- ökonomische Analyse" Munich 1992 at p.18

Nevertheless, the research so far backs up the careful assumption that the larger share of the spread between the preference and the ordinary share derives from the higher assessment of the vote instead of financial implications. This notion is also supported by an inquiry carried out by Ernst/Gassen/Pellens[73]. Here a number of shareholders stated that a preference share without voting right should have a share price that is on average 20% cheaper than that of an ordinary share (Figure 3)[74].

Figure 3: Inquiry result on the question: How much has a Preference Share without Voting Right to be cheaper compared to an Ordinary Share?



In conclusion, the voting right has a measurable value. This supports the fact that shareholder engagement, beyond corporate governance, has (providing it is carefully used) a positive impact on the equity price. The constant stronger price for shares with a voting right provides a sound argument in favour of shareholder engagement positively influencing stock prices. A useful example in this respect is the MLP AG. In 2001, they decided to change ordinary shares into preference shares in a ratio of 1:1. In the following year the AGM quorum (Figure 6) dropped by 24%, while the stock price suffered considerably.

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73 Ernst, Edgar/Gassen, Joachim/Pellens, Bernhard „Verhalten und Präferenzen deutscher Aktionäre - Eine Befragung privater und institutioneller Anleger zu Informationsverhalten, Dividendenpräferenz und Wahrnehmung von Stimmrechten" Studies of the Deutsche Aktieninstitut (German Institute to Promote Shareholding), Frankfurt January 2005, Issue 29 to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm

74 Ernst, Edgar/Gassen, Joachim/Pellens, Bernhard „Verhalten und Präferenzen deutscher Aktionäre - Eine Befragung privater und institutioneller Anleger zu Informationsverhalten, Dividendenpräferenz und Wahrnehmung von Stimmrechten" Studies of the Deutsche Aktieninstitut (German Institute to Promote Shareholding), Frankfurt January 2005, Issue 29 to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm at p.29 and 37

2.2.6. The Impact of Legal Actions

No direct empirical evidence exists showing an impact on the stock price caused by legal actions a shareholder pursues in a German court (e.g. appeal against a resolution or nullity action). Here it could only be assumed that an action brought forward by a shareholder has a negligible negative effect on the stock price (in contrast to class action in the US) as the value in dispute mostly remains within reasonable limits (providing the company is not charged with fraud). However, if the action by the individual investor or group of investors is permissible and justified, then a settlement payment or a ruling by the court could have a considerable positive effect for them.

As no empirical evidence exists for the German financial market the mentioned impacts are only of theoretical nature.

2.3. Shareholder Engagement and Intangible Purposes of Action Taken by Investors

Having given some indications that shareholder engagement could have a measurable positive effect on the equity price; intangible purposes of action taken by investors need to be taken into consideration. As it has been stated above and will be explained in detail below, social responsible investment (SRI) or sustainable asset management, which describes the same investment policy, is becoming increasingly important to investors. While in the US this type of shareholding already achieves about 13%[75], the share in Germany is considerably lower with 0.4%[76]. The reason for this huge discrepancy is the difference in approach. In the US, a fund is categorised as an SRI when investments into companies linked with weapons of mass destruction, child labour, tobacco or environmental pollution are excluded. In Germany the definition of sustainable asset management is far narrower. According to the definition of the "Forum Nachhaltige Geldanlagen"[77], sustainable investments are investments which beyond economical factors also consider social and ecological criteria[78].

The nature of this investment philosophy usually implies that socially responsible investment will in turn produce greater shareholder engagement. The clients of SRI funds often do not only have a strict investment policy, but are also active shareholders, sometimes even with an own voting policy.

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75 Loew, Thomas „Internationale Entwicklung der Regulierungen zur Förderung ökologisch-ethischer Finanzdienstleistungen" Discussion Paper of the Institut für ökologische Wirtschaftsforschung 56/02, Berlin 2002 to download at www.ioew.de/home/downloaddateien/DP5602.pdf at p.48

76 Loew, Thomas „Internationale Entwicklung der Regulierungen zur Förderung ökologisch-ethischer Finanzdienstleistungen" Discussion Paper of the Institut für ökologische Wirtschaftsforschung 56/02, Berlin 2002 to download at www.ioew.de/home/downloaddateien/DP5602.pdf at p.31

77 Forum Nachhaltige Geldanlagen is the largest German association promoting sustainable investments - www.forum-ng.de

78 Forum Nachhaltige Geldanlagen "Nachhaltige Investments" to download at http://www.forum-ng.de/upload/Mitglieder-log-in/Definitionenfinal05-10-28.pdf

It is incomprehensible that some SRI funds see voting their stocks not as a SRI engagement as it only plays a minor role[79]. More importance is seen in dialogues with the issuers. This attitude is inconsequent and dangerous. An asset manager of a sustainable fund, who promotes an advanced form of investment and therefore applies strict standards to the issuers, appears implausible when ignoring the fiduciary responsibility he has towards the beneficiary owners.

The fact that not only institutional SRI investors but also private investors show an engagement in some political issues is certainly worth mentioning. With respect to this kind of activity, it is problematic that the suggestions private investors offer in the general meeting are badly prepared and poorly presented. Hence, even though they might have excellent points they do not have a chance to succeed or at least being considered by the management.

Unfortunately, it has not yet been investigated if shareholder proposals with a socially responsible background are more successful and if management is more receptive of these compared to other economic topics.

2.4. Shareholder Engagement versus Stakeholder Interest

The corporate interests of shareholders on one side and stakeholders on the other are mostly diverging. This finding is not new and led to a "shareholder versus stakeholder" debate[80]. A good catchphrase in this respect is "shareholder value". It is still associated with corporate policy aiming at short-term profit maximisation, and thus should have a negative impact on the interests of stakeholders. They are concerned about the company's social responsibility, which is only achievable through long-term profit maximisation. According to the International Center for Corporate Social Responsibility (ICCSR)[81], corporate social responsibility refers to the attention of business to community involvement, socially responsible products and processes and socially responsible employee relations.

However, the discussion on shareholder value versus corporate social responsibility is not a central part of this thesis. The question if codetermination rights of stakeholders should be expanded is not discussed in this thesis, either. Both issues are wide-ranging and thus provide ample material for a thesis in itself.

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79 Eurosif: Socially Responsible Investment among European Institutional Investors – 2003 Report to download at http://www.eurosif.org/pub2/lib/2003/10/srirept/eurosif-srireprt-2003-all.pdf at p.50

80 Sources: Schmidt, Reinhard H./Weiß, Marco „Shareholder vs. Stakeholder: Ökonomische Fragestellungen" Working Paper Series Finance and Accounting No. 104, January 2003 to download at www.wiwi.uni-frankfurt.de/schwerpunkte/finance/wp/770.pdf; Aabo, Tom "Ownership and Risk Management: Shareholder versus Stakeholder Satisfaction" Competitive Paper, Aarhus/Denmark 2002 to download at www.aueb.gr/deos/EIBA2002.files/Papers/C73.pdf; Cornelius, Peter/Kogut Bruce "Creating the Responsible Firm: In Search for a New Corporate Governance Paradigm" in German Law Journal No.1 (1st of January 2003) to download at www.germanlawjournal.com/article.php?id=224

81 International Center for Corporate Social Responsibility (ICCSR) at http://www.nottingham.ac.uk/business/ICCSR

The question to be solved with regard to this thesis is whether shareholder engagement collides with the stakeholders' interest. Having indicated the underlying conflict, it appears that activities by investors will also have a negative impact on corporate social responsibility.

Undisputedly, shareholders are interested in a good stock price development. They try to achieve this by engaging and targeting good corporate performance. Although the shareholders' sphere of activity is limited, as they are only able to articulate their interests by negotiating, asking, voting, suing or most important by selling their shares, their influence on corporate decision making could still be considerable. The examples of capital increase, altering the statutes, or approving takeovers alone indicate the significance of shareholder engagement. For these reasons, it becomes obvious that shareholder engagement could in some areas collide with the interests of stakeholders. This cannot be ignored.

However, there are also some indications showing that shareholder engagement does not necessarily conflict with stakeholders' interest.

In approaching this issue, it is first of all important to recognise that an active shareholder is interested in a healthy company and shareholder value, which could be assumed as he accepts expenses (e.g. costs for proxy voting) in order to raise his voice[82]. Although this realisation might more be the result of legal requirements (e.g. in Germany § 32 s.1 s.3 InvG – Kapitalanlagegesellschaften should vote) than of conviction, it has to be noted positively that the shareholder lets management know that it needs to do better.

Additionally, a differentiation needs to be made between an active investor and a speculator. Usually the latter does not get involved in corporate policy. His aim is to make profits in a short period of time. Therefore, he tries to keep expenses as low as possible and will typically sell his shares instead of getting involved in company business.

Another indicator that shareholder engagement is not automatically interfering with the interests of the stakeholders is the scope of their engagement. As it can be seen in the Figure 4 and 5, the stakeholder is not primarily focused on profit maximisation. A number of issues like corporate governance, remuneration or takeover defences are not or only partially value related.

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82 Hirschman defines the concept of voice as "any attempt at all to change, rather than to escape from, an objectionable state of affairs", in Hirschman, Albert „Exit, Voice and Loyalty: Responses to Decline in Firms, Organisations and States " Harvard University Press, Cambridge 1970 at p.30

Figure 4: Question for Issuers: Which issues have investors asked to discuss or most often voted on?[83]

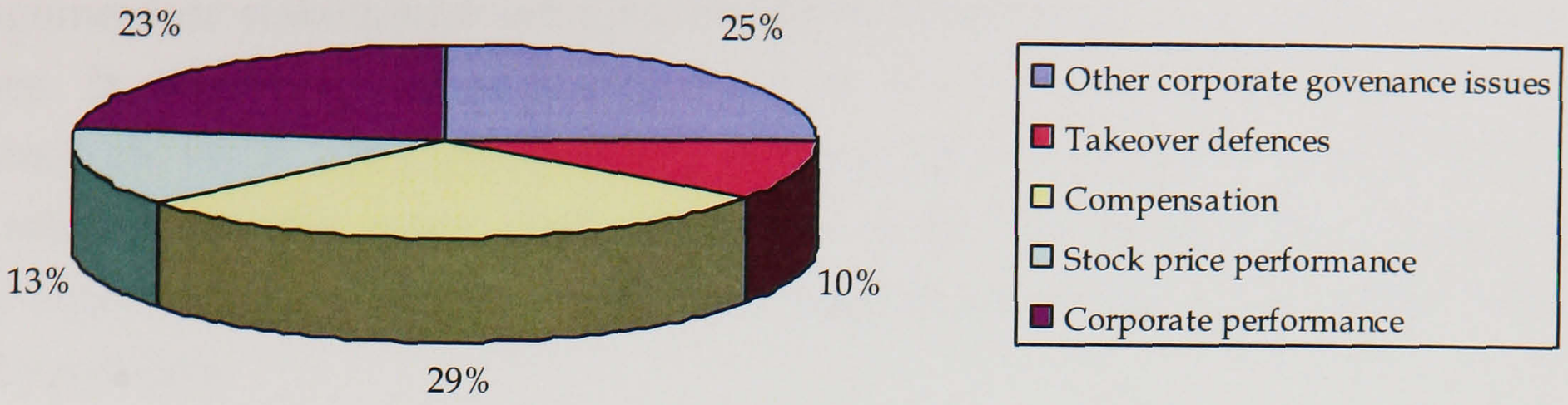
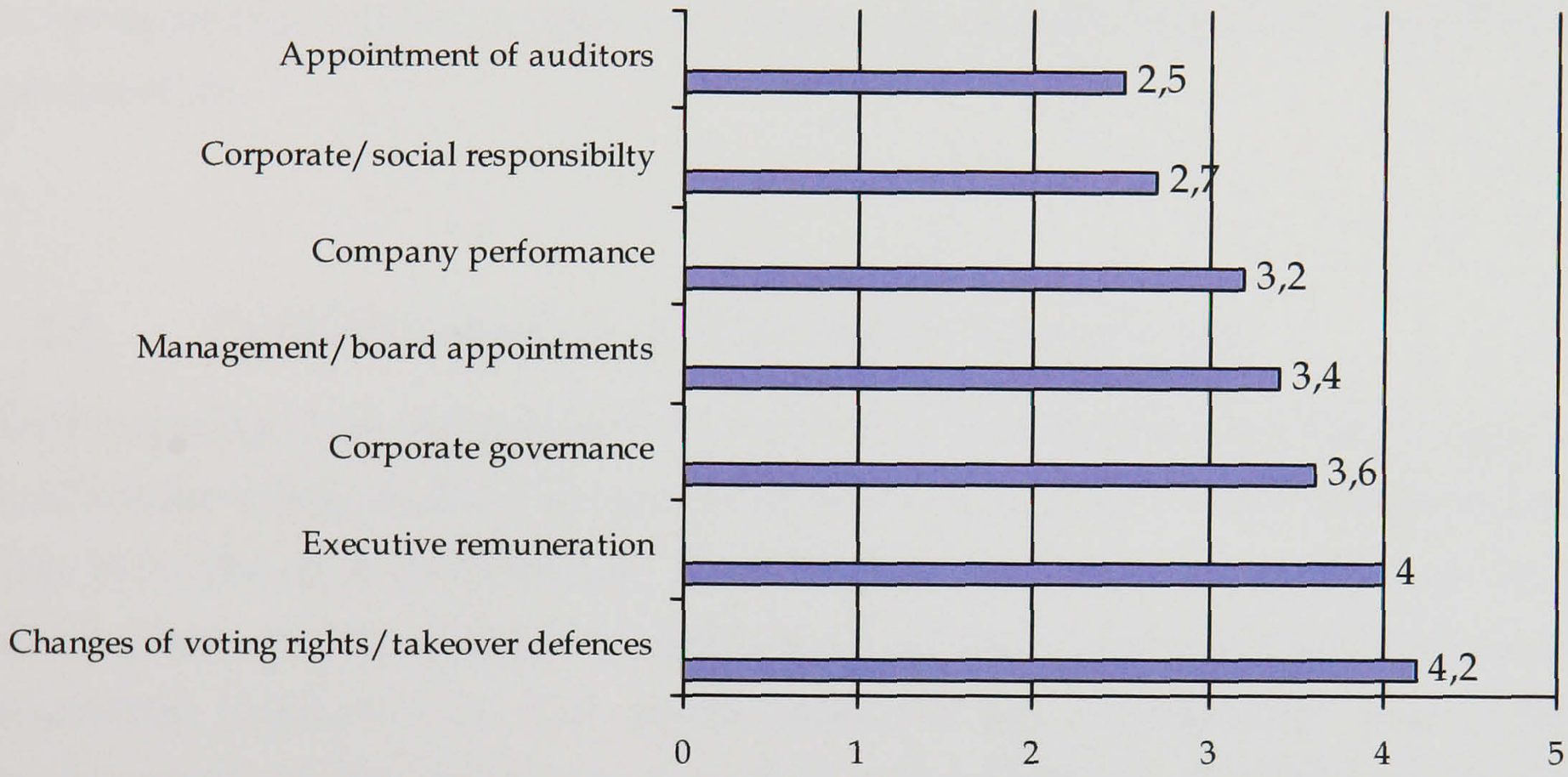


Figure 5: Question to Investors: Which type of issues are you most likely to want to discuss or vote on?[84]



Taking this into account, a conflict of interests between active investors and stakeholders is not as obvious as it seemed to be in the first place. There are some indicators showing that shareholder engagement targets issues, which could also be attributed to the stakeholders' interest. To mention in this respect are excessive remuneration of management; corporate/social responsibility; corporate governance or the common interest to reduce the likelihood of destabilising financial meltdowns.

The existence of some common interests should not obscure the fact that engaged shareholders and stakeholders have conflicting concerns. In these cases it is important that the board could function as an arbitrator, as it is management which is mostly better positioned to assess facts, circumstances and developments. It is only natural that shareholders as well as stakeholders primarily focus on their own benefit rather than that of the company. Therefore equilibrium of the different interests needs to be maintained. For instance, a tip over could result in a reduced equity price or in a strike.

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83 Grubaugh, Richard H. „Survey of Global Voting Trends" 2004 at p.20 to download at www.iirf.org (International Investors Relation Federation)

84 Grubaugh, Richard H. „Survey of Global Voting Trends" 2004 at p.19 to download at www.iirf.org (International Investors Relation Federation)

Such a development needs to be avoided as it contradicts the interest of the corporation. Taking this into account the question should not be whether to favour shareholder engagement or stakeholder interests but how to establish an equilibrium benefiting all parties. It should be considerably easy to achieve this goal. Engagement usually becomes an issue with shareholders seeking long-term profit maximisation. This is exemplified by the costs and efforts in order to pursue the engagement. The perseverance that is necessary until the engagement begins to take effect also supports this hypothesis.

In conclusion, the conflict between shareholder engagement and stakeholder interests should not be overestimated as it has been done in the "shareholder versus stakeholder" debate. There are sufficiently common interests, which give allowance to the opinion that under certain circumstances shareholder engagement is beneficial for stakeholders.

2.5. Critical Evaluation of Shareholder Engagement

While arguing that engagement by investors is beneficial for the company and fosters shareholder value, it must be accepted that engagement can be abused. Indeed this has often been the case in Germany, inflicting varying degrees of damage on the company and its price. An inaccurate picture of the company can be drawn because of thoroughly reasonable criticism on the profit maximising, sustainable, and ethical or other development of the company voiced in an aggressive, inadequate or sensationalistic way.

Far-reaching shareholder engagement also has the potential to harm other shareholders or the issuer. Having laid the focus on Germany, reference should be made to issues like the abuse of the right to file a suit (Chapter 6.2.6.1.7.), the danger of accidental majority outcomes, misdirected majorities (Girmes AG – Chapter 2.2.2.), driving a campaign against the CEO (e.g. Wyser-Pratt versus IWKA AG in 2005) or other negative effects. Due to the lack of self-regulation of the capital market and due to structural overregulation by the legislator, loopholes for the abuse of shareholder rights have been created in Germany, as I will elaborate later in this thesis. This does not necessarily need to be the abuse of an action taken in order to achieve a tidy settlement; it could also involve insider trading and other activities, which are capable of harming the interests of shareholders or substitutable stakeholders. The essentially positive impact of shareholder engagement can quickly become a lasting negative state of affairs, or even destructive.

The necessity of sound regulation for shareholder engagement is as crucial as self-control pursued by the investors. Additionally, the management and supervisory board

need to react when recognising an abusive behaviour. Accidental majorities, uncontrolled squeeze-outs, unjustified blocking, etc. must be avoided.

2.6. Concluding Assessment

We have seen that a number of different approaches offer varying results on the impact of shareholder engagement. It has been shown that an investment strategy focused on good corporate governance, could not only reduce risk, but also deliver returns that could be two-digit percentages higher compared to investments renouncing this strategy.
However, in reviewing these approaches with respect to the impact of shareholder engagement three issues become obvious.

The emphasis is placed squarely on negotiations, proposals and voting. This derives from the beneficial effect these forms of engagement could provide to the company and its investors. Results on the impact of shareholder engagement regarding information request, speaking at the general meeting and litigation could not be provided. This is not very surprising with regard to information inquiry or speaking at a general meeting. Yet it is necessary to mention that, in contrast to the US, actions a shareholder pursues in a German court (e.g. appeal against a resolution or nullity action) rarely show effects, as the paid settlement does not put a real strain on the stock price.

Second, the price difference between shares with and without voting right is not, or only to a limited extent, influenced by the shareholder. Hence, this effect is more of an investment tool than the result of shareholder engagement.

Third, the great difference of the tools and studies on the stock price derives from the varying approaches in time, scope, region, shareholder groups, and other parameters. However, the vast majority of methods allow the statement that shareholder engagement has a more or less positive effect on the stock price.

To draw a conclusion shareholder engagement, in Germany as well as globally, has a positive effect on the stock price development. Due to the great diversity in the results of the different approaches, it is not possible to provide a universally applicable formula. Shareholder engagement can also positively affect non-financial issues, like social responsibility. Moreover, shareholder engagement is not necessarily in conflict with the interest of the stakeholders. Overall, it is certainly valid to state that the success for the shareholders is to a great extent dependent on excellent negotiation skills, good tactics and functional shareholder communication.

Finally, it needs to be pointed out that shareholder engagement generates its value by exhausting the given legal tools and the usage of complementary steps. Consequently it is able to enrich the existing corporate model in Germany.

Having shown the benefit of shareholder engagement, I will now turn to examine its realisation in corporate Germany. In doing so, the "hierarchy" of forms of engagement set out in Chapter 1 will be employed. Chapter 3 begins this process by providing an overview of the current situation in Germany.

Part B - Descriptive Part

3. Chapter: Support for Shareholder Engagement

An examination of the instruments supporting shareholder engagement is necessary to understand its still existing deficits and to develop a healthy activity according to the introduced hierarchy (Chapter 1.2.). The means to support shareholder engagement could help to direct their activity into the correct and efficient channels, or could anticipate necessary actions.
Therefore this chapter will explain the support investors could expect from third parties in pursuing sound shareholder engagement. I will provide an insight into the role of the supervisory board as the shareholder representatives' body on the board and the possibilities proxy solicitation could offer; therefore looking beyond the general meeting and the provided hierarchy of shareholder engagement.

3.1. The Supervisory Board as the Extended Arm of the Investors

In the German corporate governance system the board is divided into the management and the supervisory board. This "German Solution" often is criticised in particular for its codetermination (50% of the supervisory board members are shareholder representatives, 50% are employee representatives). Some examples, like that of Volkswagen in 2005[85] certainly justify a careful approach to this system.
The principles of this model are still seen as an alternative for other judicial systems, which view their shareholder representation to be in need of reform. In particular the European Union, in its efforts to create the Societas Europea, took into account the division of the supervisory board and the management board[86]. This assessment is underlined by the Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe – the "Winter-Committee", which came to the conclusion that neither one-tier nor two-tier board structures are intrinsically superior: each may be the most efficient in particular circumstances[87].

To gain an understanding of this concept it is essential to assess the value of the supervisory board for shareholder engagement. In general the duty of the supervisory board is to oversee the activity of the management board (§ 111 s.1 AktG). According to

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85 Volkswagen invited some employee representatives to „pleasure trips". The latter are also suspected to have taken bribe money – Source e.g. Ritter, Johannes "VW-Affäre – Sexbelege und Lügengeschichten" in Frankfurter Allgemeine Zeitung 16.11.2005, No.267 at p.2

86 Blanquet, Franҫoise "Das Statut der Europäischen Aktiengesellschaft (Societas Europea "SE")" in Zeitschrift für Unternehmens- und Gesellschaftsrecht ((ZGR)) January 2002 31.Volume number 1 p.20-65 from p.21ff

87 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" 2002 to download at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf at p.8

Hüffer, this supervision consists of a control of management. It needs to be applied to the past, must include participation in management tasks through consultation (preventative governance) and must be legal, proper and suitable[88]. This responsibility is supplemented by the possibility to influence the business of the corporation to a certain extent[89]. This influence is exerted through appointment and employment of the management board members; engaging the auditors in charge; coordination with the management board as to how annual accounts and the profits are utilised; writing reports; and developing resolution proposals for the general meeting.

In contrast to other judicial systems (e.g. U.K. – Section 1 A.4 of the Combined Code 2003[90]) where non-executive directors are appointed by a nomination committee, shareholders of German Aktiengesellschaften could get engaged in the election of the supervisory board members in the general meeting (§ 19 s.1 s.1 AktG).
Their usual tenure is five years, but they may be re-elected. One of the tasks of the members of the supervisory board is to make suggestions for new board members to be appointed[91]. The sensitive work of finding a qualified substitute for the supervisory board should not be left to the general meeting for good reasons. It is necessary that the search for a member of the supervisory board is professionally organised. This is not guaranteed when the suggestion right is left completely to the AGM. The supervisory board member needs to be qualified and experienced in matters of corporate governance and should be elected because of these characteristics, not because he carries the sympathies of the shareholders.

The investors, nevertheless, also have the right to make their own proposal to the general meeting[92]. Their recommendation has a very limited chance to succeed, because institutional investors especially prefer to follow the advice of the supervisory board rather than that of private shareholders. However, it would certainly be beneficial if more than one suitable candidate stood for a place in the supervisory board. Having a choice between three or four candidates will indisputably promote competence rather than reflect a good network or lobby.
However, it will be interesting to see whether specialised consultants will slowly take over the nominations for supervisory board members. This may occur as the standards for a supervisory board member get increasingly complex and require professional experience. Additionally, international shareholders need to be represented on the board – the existing mechanisms can only implement this to a limited extent.

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88 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 111 No.4ff

89 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.346

90 "The Combined Code on Corporate Governance", 2003 to download at http://www.fsa.gov.uk/pubs/ukla/lr_comcode2003.pdf

91 Happ, Wilhelm „Aktienrecht Handbuch - Mustertexte - Kommentar" 2nd Edition Cologne, Berlin, Bonn, Munich 2004 at p.812

92 Happ, Wilhelm „Aktienrecht Handbuch - Mustertexte - Kommentar" 2nd Edition Cologne, Berlin, Bonn, Munich 2004 at p.813

According to § 110 s.3 s.1 AktG the supervisory board must at least meet twice a year. Although the German Corporate Governance Code dictates that a member of the supervisory board should not have more than five mandates, this rule is not widely obeyed to this point in time. Ten mandates are still not unusual, which is the maximum according to § 100 s.2 s.1 No.1 AktG.

The supervisory board consists of shareholder representatives, who are elected by the annual general meeting (§ 119 s.1 s.1 AktG) and employee representatives[93]. This right of codetermination in stock corporations means that in an enterprise with more than 2.000 employees, the latter have the right to contribute half of the members to the supervisory board. Control remains with the shareholder representatives as their chairman's vote counts twice in case of a deadlock. However, it seems that the huge employee representation on the board results in a model that is geared towards harmony and the willingness to compromise, instead of one that pursues effective and qualified corporate governance. This does not necessarily mean a negative outcome as Breuer, former CEO of the Deutsche Bank, reports:

> "The codetermination has produced really good results in manifold ways, especially in difficult times. I have been a member of supervisory boards, where particularly the employee representatives distinguished themselves by showing constructive, professional, fast support for drastic rescue measures, when the existence of the enterprise was endangered. [...] The model of codetermination has to be supported and presents an important achievement.[94]"

Nevertheless, he continues with criticism of the current state of employee representation: The fact that only German employee representatives are allowed on the boards even when the majority is employed abroad might lead to decisions not based on economical, but also on local and political issues[95].

Therefore, the role of the supervisory board as the shareholders' corporate governor in the German system is double-edged. This is based on the two-tier boards of the legal system, separating management and supervisory boards.

Additionally, the corporate crossholding (see Chapter 4.1.3.) structure plays an important role. Still, a number of companies own a considerable share in other companies (e.g. Münchner Rück owns 4,9% of Allianz, Allianz owns 9,8% of Münchner Rück, Deutsche Bank owns 4,4% of Daimler Chrysler, Daimler Chrysler owns 30,2 of EADS[96]). This is particularly the case with banks and insurance companies, but also with large private investors. Consequently, the nexus of members in the different supervisory boards is almost symbiotic to the crossholdings. With the corporate

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93 § 76 Betriebsverfassungsgesetz, § 5 Mitbestimmungsgesetz

94 Breuer, Rolf.E. "Corporate Governance börsennotierter Banken" Documentation of the Seminar "Corporate Governance - Nutzen und Umsetzung" organised by the Deutsche Aktieninstitut on the 12th of March 2001: to download at http://www.dai.de/internet/dai/dai-2-0.nsf/LookupDL/41256A99002BDD55C1256A5E002C4E1F/$File/Studie_15.pdf at p.24

95 Baums, Theodor „Corporate Governance - Aktuelle Entwicklungen" 2003 to download at http://www.irp.uni-trier.de/12_Baums.pdf at p.8

96 Source: Insight - Corporate Governance Germany "Insight Shareholder ID" Issue 0/2006 at p.24f

investor mostly being the largest single shareholder, his place on the supervisory board is almost reserved. This means that for other shareholders it is extremely difficult to bring forward alternative candidates, who are not connected with a bank, a corporate investor or the major private shareholder. This is certainly problematic as it means that mandates are "conferred" according to the proportional representation and not according to qualification[97]. What is even worse is that the supervisory board is a potential pool of conflicts of interest. Being provocative, the independence of the members of the supervisory board is questionable. The background of some members supports this assertion. For example associates, who are sent by banks, could be tempted to protect the position of their employer as a creditor by looking for new business opportunities, rather than acting in the interests of the shareholders[98]. The same can be applied to employee representatives. Members, who are associated with trade unions[99], often have to choose between the interests of their union, the employees or the corporation[100].

Criticism is not only justified regarding the composition of the board, but also regarding its organisation and its status. Sherman points out that a seat in the supervisory board is often abused as a farewell retirement present for long-serving managers, union members or anyone else who might need to be rewarded with a lucrative position[101]. With regard to the workload of some supervisors, who have a seat on ten boards besides their job as a CEO and other honorary posts, the investment of time is certainly limited. Therefore it is not uncommon that the members meet only four times a year and then only for two hours. The reproach that the supervisory board is a type of Breakfast Club is not without foundation.

The German Corporate Governance Commission (Cromme-Commission) reacted to some of these issues and consequently, tried to improve the independence of the supervisory board with the latest alteration of the German Corporate Governance Code[102]. Special attention should be drawn to the recommendation that the former CEO of a company should not automatically become chairman of its supervisory board. If the company insists on this changeover it needs to justify this intention explicitly in the

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97 Brost, Marc/Heuser, Uwe Jean „Das sind absurde Zustände" Interview with Hilmar Kopper in „Die Zeit" 18th Issue 2001to download at http://www.zeit.de/2001/18/Wirtschaft/200118_beistueck_corpor.html

98 During the takover battle between Thyssen and Krupp in 1997 the Deutsche Bank was consulting Krupp, while they also had a member in the supervisory board of Thyssen.

99 Schmidt, Karsten "Gesellschaftsrecht" 4th Edition Cologne, Berlin, Bonn Munich 2002 at § 28 III No.4 a)

100 A famous example is the role of Bsirske (Chairman of Verdi, the largest union worldwide): In 2002 he initiated a labour dispute about the compensation of Lufthansa workers on the ground, although he was a member of the supervisory board of the airline. The dispute lead to a loss of the Lufthansa stock price. Anyway, at the end the general meeting refused his discharge. A Financial Times Deutschland article on that Issue: „Lufthansa-Aktionäre strafen Bsirske ab" www.ftd.de/ub/di/1055680383285.html?nv=sl

101 Shearman, John „Germany – Controlling Directors the German Way" in The Company Lawyer Vol.18 No.4 (1997) p. 123-125 at p. 123

102 Third Alteration of the German Corporate Governance Code: 02.06.2005

general meeting[103]. A similar provision is also stated in the Combined Code[104] in the U.K. where Section A.2.2 states that a CEO should not go on to become chairman. Just like in Germany an exception is also possible providing that major shareholders have been consulted and it has been explained in the annual report.

Although the supervisory board acts as the extended arm of the shareholder, the legal engagement of the investor according to the claimed hierarchy is limited to its election (en bloc or single[105]); the ability to file a suit due to an improper election process; and the relief from office (§ 103 s.1 AktG).

From a shareholder engagement point of view it would be of interest if the board was able to take over an active role in "shareholder negotiations"[106] on corporate governance issues. Currently investors are negotiating their issues directly with the management without consulting their board representatives. From an objective point of view the supervisory board is a redundant intermediate. The latter represents the shareholders, but as the controller of the management board it is also involved in the day to day business of the corporation. Therefore the supervisory board members are in a perfect situation to evaluate the issues from both sides. However, if being an intermediate in shareholder negotiations with management becomes one of their future tasks, the legislator does not necessarily need to reform the supervisory board system. The possibilities of the existing law need to be exhausted, while the compliance with the Corporate Governance Code should be supervised and supported, rather than enforced.

In conclusion, the role of the supervisory board as the extended arm of the shareholders has improved over the last couple of years, because of an increased awareness of the investors and an active legislator. Although the supervisory board has not yet come up to a status which will guarantee the shareholders sound corporate governance, the current discussions about codetermination and the new requirements by the Corporate Governance Code are pointing in the right direction.

3.2. Proxy Solicitation

Increasingly, issuers hire proxy solicitors. Their role must not be confused with the completely different role of a "lawyer". The main business field of the proxy solicitor is the tracking of investors. Here it has to be acknowledged that not only do they serve the

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103 Kirschbaum, Tom „Deutscher Corporate Governance Kodex überarbeitet" in Der Betrieb Heft 28 Vol. 58 (15.07.2005) p. 1473-1477 at p.1473

104 "The Combined Code on Corporate Governance", 2003 to download at http://www.fsa.gov.uk/pubs/ukla/lr_comcode2003.pdf

105 More on that issue: Segna, Ulrich „Blockabstimmung und Bestellungshindernisse bei der Aufsichtsratswahl" in Der Betrieb No.21; 21.05.2004 p.1135-1137

106 For Shareholder Negotiation see chapter 6.1.

issuer but also the shareholder. This is possible as they are free of conflicts of interest. Their task is to contact the shareholders and not to offer analysis or advice.
Proxy solicitation is of greatest value when a company decides to change from bearer shares to registered shares. As in this case the beneficial owner of the shares is not known by the company, measures must be taken to secure that the transformation of the shares is successful. Another advantage is that the data, which are collected by the proxy solicitors, enable the issuer of bearer shares to improve his investor relations. In addition to that companies engage their services to bring shareholders to the ballot box. By doing this, the issuer ensures high capital presence at the general meeting and thus reduces the chances of accidental majorities as well as the danger that the investor will sell his shares rather than raising his voice when issues within the company put the stock price under pressure. Hence, by hiring a proxy solicitor, such as Georgeson Shareholders, the issuer is also encouraging and improving shareholder engagement.

The proxy solicitor also plays an important role when an investor wants to carry out a proxy contest or proxy "fight"[107]. This is seen, for example, in connection with a hostile takeover. A proxy contest occurs when the acquiring "predator" company attempts to convince shareholders to use their proxy votes to install new management that is open to the takeover. The technique allows the predator to avoid paying a premium for the target.
A famous example in this respect is the takeover battle between Hewlett Packard and Compaq. Both the objecting party as well as the supporting party hired proxy solicitors in order to win the decisive majority of shareholders for their side.
On the assumption that shareholder engagement in Germany will increase and the use of registered shares will continue in the next years, the role of proxy solicitors will become more and more important in the future.

To recap, we have examined the means of support for shareholder engagement focussing in particular on the role of the supervisory board and proxy solicitation. Examining this helped us to understand the supporting environment beyond the offered hierarchy of shareholder engagement.

107 Definition of Proxy Contest: to download at www.investorwords.com/3921/proxy_contest.html

4. Chapter: Empirical Evidence on Shareholder Engagement in Germany

To allow a better understanding of the extent to which shareholder engagement is practised in Germany, some empirical data will be provided[108]. The latter concentrates on the issues of voting and litigation. For all other measures numerical information hardly exists, if at all. This primarily derives from the "hidden" character of these activities and the difficulty to assess the background of the engagement. Consequently, the focus has been on the right to vote and the right to file a suit.
Moreover, based on the empirical results it is the issue of voting that causes greatest concerns.
The figure below shows that in the last seven proxy seasons the presence at AGMs held by DAX 30[109] companies on average constantly decreased, from nearly 61% in 1998 to less than 46% in 2005. Here Infineon Technologies AG achieved the lowest recorded capital presence of only 17.59%.

Figure 6: Capital Presence at DAX 30 AGMs (1998-2005) in Percent of all Shareholders[110]

	in the DAX since/until	Current Index	1998	1999	2000	2001	2002	2003	2004	2005	3-Year-Average
Adidas-Salomon AG	since 19.06.98	DAX	*35,10*	43,90	45,44	30,00	31,52	23,17	28,25	26,94	26,12
Allianz Holding AG		DAX	70,92	69,06	60,60	53,70	46,71	39,97	37,15	34,82	37,31
Altana AG	since 23.09.02	DAX		*76,00*	*71,71*	*65,21*	*Ca. 64,00*	63,00	67,22	64,78	65
BASF AG		DAX	53,03	49,48	46,02	43,59	36,82	31,31	34,99	34,39	33,56
Bayer AG		DAX	47,53	44,79	37,53	35,90	33,21	36,00	35,50	35,91	34,8
Bayerische Hypo-Vereinsbank AG *		DAX	64,10	59,10	51,99	53,48	57,39	55,56	49,88	53,4	52,95
BMW AG		DAX	73,00	73,00	64,40	64,04	66,57	65,84	63,70	55,04	61,53
Commerzbank AG		DAX	46,54	43,91	55,97	56,07	58,93	57,31	46,53	39,39	47,74
Continental AG	since 22.9.03	DAX	-	-	-	-	*41,66*	33,57	34,44	23,55	30,52
DaimlerChrysler AG **		DAX	63,97	39,02	39,00	36,92	38,25	38,84	43,69	37,84	40,12
Degussa AG ***	until 23.09.02	MDAX	69,51	70,86	82,82	75,86	76,24	-	-	-	-
Deutsche Bank AG		DAX	44,69	37,50	31,73	34,44	33,41	38,75	31,98	25,47	32,07
Deutsche Börse AG	since 2003	DAX					-	44,53	31,55	59,76	45,28
Deutsche Lufthansa AG		DAX	31,90	34,60	35,25	34,90	41,14	46,37	41,09	41,4	42,95

108 Figure 5, 6, 10, 11, 15, 17, 20, 21, 23, 24, 30

109 Index of the 30 biggest public listed companies in Germany

110 Source: Deutsche Schutzvereinigung für Wertpapierbesitz e.V. (German Association for Share ownership) to download at www.dsw-info.de/uploads/media/HV-Praesenz_2005.pdf

Deutsche Post World Net AG	since 19.03.01	DAX	-	-	-	76,18	77,37	79,35	72,71	74,19	75,42
Deutsche Telekom AG	since 18.11.96	DAX	85,61	82,67	75,86	69,52	56,45	59,47	63,53	54,47	59,16
Dresdner Bank AG	until 23.07.01		70,33	61,72	59,75	-	-	-	-	-	-
E.ON AG	since 19.06.00	DAX	-	-	-	39,01	37,35	31,00	35,00	29,92	31,97
Epcos AG	until 2003	DAX	-	-	42,60	44,88	54,54	-	-	-	-
Fresenius Medical Care AG	since 17.09.99	DAX	*62,40*	*67,88*	64,79	61,06	62,59	64,97	65,00	63,8	64,59
Henkel AG (Vz.)		DAX	65,12	66,75	83,24	84,50	83,73	79,39	80,22	78,31	79,31
Hoechst AG	until 17.09.99		*65,86*	*62,68*	-	-	-	-	-	-	-
Infineon Technologies AG	since 19.06.00	DAX	-	-	-	74,74	41,66	31,88	17,59	48,19	32,55
Karstadt-Quelle AG	until 19.03.01	MDAX	*64,90*	*65,65*	*68,46*	-	-	-	-	-	-
Linde AG		DAX	59,00	56,46	54,4	53,67	54,19	50,08	50,72	49,75	50,18
MAN AG		DAX	61,00	59,81	55,80	50,62	52,80	48,41	45,51	34,31	42,72
Metro AG ****		DAX	78,49	77,72	87,53	66,93	66,38	65,86	65,27	67,4	66,18
MLP AG	until 2003	MDAX	-	*77,89*	*79,22*	75,38	51,41	59,50	-	-	-
Münchener Rück AG	since 20.09.96	DAX	75,80	72,33	69,80	65,60	53,45	57,49	44,89	42,49	48,29
RWE AG		DAX	75,01	67,15	63,90	65,09	66,08	39,06	59,03	56,52	51,54
SAP AG (Vz.)	since 15.09.95	DAX	59,77	53,36	56,70	50,85	55,37	58,04	59,53	54,04	57,2
Schering AG		DAX	43,16	47,01	43,33	37,40	37,00	34,84	33,29	32,62	33,58
Siemens AG	since 18.03.99	DAX	46,66	44,97	24,93	22,00	36,40	47,51	32,67	32,15	37,44
ThyssenKrupp AG *****		DAX	58,74	55,90	64,13	61,26	59,97	61,60	56,18	54,03	57,27
TUI AG (former Preussag)	since 03.09.90	DAX	65,41	66,87	39,30	37,21	37,21	54,18	54,30	37,18	48,55
Veba AG ******	until 17.06.00		*45,33*	*46,44*	*40,41*	-	-	-	-	-	-
Viag AG ******	until 17.06.00		*66,39*	*54,99*	*65,47*	-	-	-	-	-	-
Volkswagen AG		DAX	43,70	37,62	34,39	36,99	32,98	29,01	37,21	33,9	33,37
Average			60,95	56,36	54,85	53,03	51,23	49,14	47,29	45,87	47,4

* from 1999, before Bay.Vereinsbank AG

** from Dec.1998, before Daimler Benz AG

*** from Dez.2000, after merger with SKW, before Degussa AG

**** from 1997, before Kaufhof AG

***** from Dec.1998, before Thyssen AG

****** After the merger of Veba and Viag, E.ON and Infineon have been included in the Dax

The average ongoing decrease of the presence of capital in German AGMs and hence, the use of the voting right raises the danger for accidental majorities, increases the possibility that the investor sells his shares rather than becoming active and weakens the position of the management and supervisory boards.

The reasons for the low and still decreasing capital presence are manifold. First, the crossholding is slowly breaking up[111]. In Germany crossholding (compare with Chapter 4.1.3.) has been widely spread. The large share some companies had in another (e.g. Deutsche Bank held 10% in DaimlerChrysler) guaranteed a higher presence at the general meeting. The sale of those shares resulted in a decrease of large engaged blockholders to the benefit of widely held share ownership, with a lower interest in shareholder engagement.

Moreover, the custodian banks are slowly pulling out of the proxy voting business. The Volksbanken[112] as well as the Sparkassen[113] have already stopped offering representation at the general meetings. This considerably increased the effort for executing the voting right for private investors, who have their shares in custody at those banks. As the small private shareholder most probably will not change his custodian in order to have a proxy for a general meeting, the votes of small private investors having shares in custody with the Volksbanken or Sparkassen were lost almost completely.

Finally, the percentage of foreign shareholders is already considerably high, and still increasing. Naturally these shareholders rarely exercise their voting rights. However, with the reform of the German Stock Corporation Act by the UMAG[114] in 2005, a record date was introduced, which removed a system of share blocking that had existed until then. Now the 21st day before the AGM is decisive for the entitlement to vote (§ 128 s.1 AktG) and shares will not be blocked for trading anymore. Therefore, institutional investors will certainly feel encouraged to exercise their voting rights for their national holdings completely and not only partially as it was the case in the past. The wish not to block all shares and to keep a number of shares tradable or unblocked resulted in disclaiming the voting power, especially by institutional investors. Also, the European Union has recognised this deficiency and commenced formulating a directive that could be passed by the end of 2006[115]. One of its objectives is to shed the reservations of international shareholders towards engagement in foreign markets and encouraging cross-border voting.

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111 compare with Figure 12

112 § 1 Genossenschaftsgesetz (Cooperative Act): The basic idea of Volksbanken (Cooperative Banks) is the promotion of the earnings or the trade and industry of the members by means of mutual business activity.

113 Sparkassen (Savings Banks) are an institution of public law. As universal banks they usually pursue a regionally limited business activity.

114 Bundesjustizministerium "Entwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" 2004 to download at http://www.bmj.bund.de/media/archive/701.pdf

115 European Commission – Directorate General Internal Market „Corporate governance: Commission proposals to make it easier for shareholders to exercise their rights within the EU " 2006 http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/06/10&format=HTML&aged=0&language=EN&guiLanguage=en

Having shown shareholders' decreasing vote execution at general meetings, it is interesting to have a closer examination of the voting behaviour of investors themselves (Figure 30).

It rarely happens that an agenda item receives less than 95% approval. Such an overwhelming vote of confidence certainly could be an indication that there have not been crucial issues within the company in the past year and that the work of the management and supervisory board is undisputed, but this is not necessarily the case.

Taking DaimlerChrysler as an example, the voting results of the 2004 AGM do not reflect a lack of satisfaction with the management. Prior to the AGM, especially institutional investors[116] pointed out a number of issues to the CEO and the board. These issues were in relation to a constantly decreasing stock price; problems with Chrysler and Mitsubishi; the Toll Collect disaster and a suit in the US. However, despite these issues the board was discharged by the general meeting with a majority of 88%.

The reason for this voting behaviour is still mostly rooted in crossholdings and in the system of the custodian banks' omnipotent influence. Due to their roles as investor, creditor and proxy not only for private but also for institutional shareholders, their voting power is more than considerable (as will be explained in more detail in Chapter 4.1.4.). Hence, a successful vote against the management is only formulated in accordance with the custodian banks.

Furthermore, when looking at the voting results the impression emerges that the boards' proposals are already a given fact for the company. This is not quite right. If the agenda item faces too much criticism and the management fears that the general meeting will not pass it, the proposal could be removed from the agenda as it happened with the item of the revision of the management remuneration at the Daimler Chrysler AGM in 2004. Hence, the unanimous consent with the boards' proposals by the shareholders may not be as uncritical as the voting majorities indicate.

The empirical data give a hint to the topical situation of shareholder engagement in Germany: The capital presence is decreasing; majority voting results do not necessarily indicate a critical dealing with certain issues at AGMs and crossholdings and concentrated ownership are still common. Although this indicates that shareholder engagement is currently on the retreat, an optimistic approach towards this topic is appropriate, especially in view of the activity of the legislator; the ongoing corporate governance discussion particularly among institutional investors; and the possibilities that shareholder engagement provide (marketing, higher stock price, SRI, etc.)

Appeals against the general meeting[117] often have a poor outcome for the corporation. It regularly occurred that shareholders filed an appeal against a resolution, motivated not

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116 e.g. Interview with Juschus, Alexander „Daimler-Chrysler-Aktionäre haben Vertrauen verloren" in Frankfurter Allgemeine Zeitung, 05.04.2004, No.81 at p.15; Deutsche Schutzvereinigung für Wertpapierbesitz e.V. „DSW will Vorstand und Aufsichtsrat von Daimler-Chrysler nicht entlasten" 05.03.2004 to download at www.dsw-info.de/DSW_will_Vorstand_und_Aufsichtsrat.342.0.html

117 § 246 AktG

by a desire for legal rectitude, but by the thought that a settlement with the company could be of considerable financial benefit for themselves. As indicated by the table below, appeals against a resolution were constantly increasing over time. An improved awareness by the corporation, the closing of legal and organisational gaps, and initiatives by the legislator helped to lessen this abuse. With the changes in the UMAG 2005[118] (e.g. shareholders could transfer far more powers to the chairman of the general meeting to summarise and limit the time to speak and ask[119]), it can be expected that such shareholder appeals, made solely for financial gain, may cease.

Figure 7: Appeals against General Meeting Resolutions[120]

Year	Stock Corporation/ Limited Partnership on Shares	Of which are Listed	Resolution Items per GM	Appeals Against the Resolution/ Nullity Action
1980	2147	459/-	4,20	6
1981	2149	456/-	3,93	1
1982	2132	450/-	3,90	2
1983	2122	442/-	4,05	7
1984	2141	449/-	3,99	3
1985	2148	451/-	3,97	20
1986	2193	467/-	4,04	9
1987	2261	474/679	4,48	17
1988	2366	465/706	4,24	30
1989	2483	486/749	4,84	29
1990	2685	501/776	4,43	26
1991	2791	519/799	4,40	26
1992	2943	521/790	4,98	20
1993	3085	522/796	4,45	21
1994	3527	523/810	4,69	45
1995	3780	527/812	4,90	33
1996	4043	-/802	4,93	47
1997	4548	-/817	4,81	27
1998	4756	-/883	5,45	39
1999	n/a	n/a	7,76	45

118 see also Chapter 9.4.

119 Seibert, Ulrich „BB-Gesetzgebungsreport: Das Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG) kommt zum 1.11.2005" in Betriebs-Berater (BB) Vol. 60 Heft 27 (04.07.2005) p.1457-1458 at p.1457

120 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.12; Baums, Theodor/ Vogel, Hans-Gert/Tacheva, Maja „Rechtstatsachen zur Beschlusskontrolle im Aktienrecht" 2000 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.86 at p.7ff

An interesting development is observed when looking at the resolution items per general meeting (from 4,2 in 1980 to 7,76 in 1999). The numbers indicate that the general meeting increasingly plays a decisive role in corporate decision making.

To draw a conclusion, the empirical data on shareholder engagement is only expressive with regard to the voting right and the right to file a legal suit. The former indicates indifference, while the latter provides evidence of an intensive and even improper use of engagement. The developments in those two areas have been deteriorating over the last couple of years despite reforms being put in place. Other forms of shareholder activities are not numerically measurable, which does not imply that they might not be used excessively.

Having examined this empirical context, our task now is to turn to the environment within which shareholder engagement must operate. The following chapter begins to tackle this task, examining the non-legal aspects of the environment of shareholder engagement.

5. Chapter: The Non-Legal Environment for Shareholder Engagement

It has been shown that shareholder engagement could create value and that it is an essential part in Germany's corporate landscape.
Now, to obtain a comprehensive picture of the non-legal environment of shareholder engagement in Germany, it is essential to recognise and categorise the different groups of shareholders, shares, issuers and other market influencing facts. Germany shows some specific features not only with regard to Company Law but also the capital market. Examples include the bearer share, which is still far more widespread than the registered share and the nexus of crossholdings in the market place.

The definitions of corporate governance are manifold and depending on the approach, a number of views and interests can be included in this concept. Investors favour an approach which emphasises the shareholders' position, whereas an employee insists on an enhanced role of the stakeholder being included in the corporate governance definition.
Although an assessment of different corporate governance concepts will not be a component of this thesis, at least the approach of the Organisation for Economic Cooperation and Development will be stated[121], to gain an understanding of this idea. For the OECD

"corporate governance is one key element in improving economic efficiency and growth as well as enhancing investor confidence. Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and should facilitate effective monitoring. The presence of an effective corporate governance system, within an individual company and across an economy as a whole, helps to provide a degree of confidence that is necessary for the proper functioning of a market economy. As a result, the cost of capital is lower and firms are encouraged to use resources more efficiently, thereby underpinning growth. Corporate governance is only part of the larger economic context in which firms operate that includes, for example, macroeconomic policies and the degree of competition in product and factor markets. The corporate governance framework also depends on the legal, regulatory, and institutional environment. In addition, factors such as business ethics and corporate awareness of the environmental and societal interests of the communities in which a company operates can also have an impact on its reputation and its long-term success."

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121 Organisation for Economic Co-operation and Development (OECD) "OECD Principles of Corporate Governance 2004" to download at http://www.oecd.org/dataoecd/32/18/31557724.pdf at p.11 (Preamble)

Although shareholder engagement seems to play only a limited part in the concept of corporate governance according to the understanding of the OECD, it should be assessed as its key feature.
However, before turning to the purpose and duty of the general meeting as the shareholders' body, the different types of shareholders, the effects of globalisation, the types of issued shares as well as the impact of modern communication forms will be discussed.

5.1. Social Environment: Types of Shareholders

The current categorisation of shareholders aligns with their legal status: institutional, corporate, private, state, foundational or associational. This differentiation is as practical as it is easy to understand the different group of investors. Unfortunately, it does not reflect the different interests of each group nor does it allow for appropriate consideration of the various minorities.

5.1.1. Shareholder Structure

The structure of share ownership in Germany is often regarded suspiciously by foreign investors. In contrast to the systems in the UK or the US, in Germany a small number of shareholders often control blocks of more than 50 %, as it can be seen in figure 8 below.

Figure 8: Shareholder Structure (In percent of all shares in circulation)[122]

Country	Year	Private House-holds	Com-panies	State	Banks	Insuran-ce/ Pension Funds	Invest-ment Funds	Abroad
France	1977	41%	20%	3%	24%	n.a.	n.a.	12%
	1992	34%	21%	2%	23%	n.a.	n.a.	20%
	1995	19,4%	58%	3,4%	4%	2%	2%	11,2%
	1999	10,6%	20,1%	n.a.	24,9% institutional investors			36,3%
Germany	1970	28%	41%	11%	11%	n.a.	n.a.	8%
	1993	17%	39%	3%	29%	n.a.	n.a.	12%
	1995	14,6%	42,1%	4,3%	10,3%	12,4%	7,6%	8,7%
	2001	15,2%	32,5%	0,7%	13%	9,7%	13,9%	15,0%

122 Deutsches Aktieninstitut (DAI) „DAI-Factbook 2002" Frankfurt 2002 at 08.6-4.; also Steiger, Max in „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance", Baden-Baden 1999 at p.33

UK	1969	50%	5%	3%	36%	n.a.	n.a.	7%
	1993	19%	2%	1%	62%	n.a.	n.a.	16%
	1995	29,6%	4,1%	0,2%	2,3%	39,7%	10,4%	13,7%
	1998	18,1%	1,4%	0,1%	5,7%	43,3%	4,9%	27,6%
Japan	1970	40%	23%	0%	42%	n.a.	n.a.	3%
	1993	20%	28%	1%	22,8%	17,4%	2,6%	8%
	1995	22.2%	31,2%	0,5%	13,3%	10,8%	11,7%	10,3%
	2000	17,9%	26,0%	0,1%	18,6%	15,7%	2,2%	18,6%
USA	1981	51%	15%	0%	28%	n.a.	n.a.	6%
	1993	48%	9%	0%	37%	n.a.	n.a.	6%
	1995	36,4%	15%	0%	0,2%	31,3%	13%	4,2%
	2000	39,1%	n.a.	0%	1,9%	29,7%	19,3%	0,0%

Large investors in German stock corporations can be companies (e.g. Allianz, Deutsche Bank) as well as private persons (e.g. Hasso Plattner - SAP) or families (e.g. Fam. Quandt – BMW, Altana).

Additionally, German enterprises still mostly finance themselves through loans rather than through the stock market. While in France, the UK and in the US the ratio between borrowed capital and owned capital resources is roughly 1:1, in Germany the ratio is 2:1[123]. Regarding this issue German companies have acknowledged that liquidity, long-term availability of financial resources and alternatives to bank loans will become more important in the future[124]. Consequently, it is not surprising that 64% of German companies (compared to 22% in France, 29% in the UK and 22% in the US) intend to look at new ways of financing[125].

This culture of ownership concentration has developed historically and is to a certain extent a result of the peculiarities of the German pension scheme which was introduced by Reichskanzler Bismark in 1889. The German system is based on a retirement insurance scheme financed by allocation. This means that the monthly contribution of workers and employees into the pension scheme is paid out immediately to the pensioners of today. As the pension is guaranteed by the state, investing in stocks has never been widespread. In contrast to that in other countries (most notably the US and

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123 Siemens Financial Services Study carried out by Steiner, Manfred/Germain, Laurent/Hilton, Denis/Schwarz Norbert „Unternehmensfinanzierung im Fokus - Entscheider aus Deutschland, Frankreich, Großbritannien und den USA antworten", 2003 to download at http://www.sfs.siemens.de/cms/Materialbestellung/pdf/Studie_2003_de.pdf at p.22

124 Siemens Financial Services Study carried out by Steiner, Manfred/Germain, Laurent/Hilton, Denis/Schwarz Norbert „Unternehmensfinanzierung im Fokus - Entscheider aus Deutschland, Frankreich, Großbritannien und den USA antworten", 2003 to download at http://www.sfs.siemens.de/cms/Materialbestellung/pdf/Studie_2003_de.pdf at p.5

125 Siemens Financial Services Study carried out by Steiner, Manfred/Germain, Laurent/Hilton, Denis/Schwarz Norbert „Unternehmensfinanzierung im Fokus - Entscheider aus Deutschland, Frankreich, Großbritannien und den USA antworten", 2003 to download at http://www.sfs.siemens.de/cms/Materialbestellung/pdf/Studie_2003_de.pdf at p.12

the UK) the working population saves for the pension by investing in stocks either directly or, more likely, indirectly through a collective investment scheme.

However, it has to be emphasised that slowly the ownership concentration is breaking up. Here the promotion of private stock saving plans (so called "Riester Rente"), employee pension schemes (supported with lower tax liability) and other incentives by the legislator in order to ease the burdens for the actual pension scheme are the main drivers for a greater dispersion of share ownership. A contribution to this development could also be ascribed to the increased popularity to invest in the stock market, which has taken up since the Initial Public Offering of Deutsche Telekom in 1996 (Figure 13). Additionally, to increasing extent foreign shareholders invested in the German stock market and by doing so also ensured a greater diversification of the ownership structure of German companies.

The increased dispersion of share ownership was also seen necessary by a symposium organised by the Deutsche Bank and the European Corporate Governance Institute in 2002[126]: A decreasing influence of creditors and large shareholders in the progress of the tax reform and other driving forces will have a positive effect on balance as the agency conflicts between large and small shareholders, as well as between givers of borrowed capital and capital resources, could be reduced. A topical deficit in the entrepreneurial efficiency was not seen: One or two important minority shareholders could achieve a positive governance of the corporation[127].

5.1.2. Characteristics of Institutional Shareholders

Without doubt the institutional investor has become a determining factor on the stock market since the mid- to late- 1990s. As it can be seen in Figure 9 the total investments have become enormous.

Figure 9: Investments of Institutional Shareholders 1990 -2001 (in Bio. US-$)[128]

	1990	1997	2001
USA	6.875,7	15.867,5	19.257,7

126 Deutsch, Klaus "Research Notes in Economic & Statistics / Corporate Governance in Deutschland - Perspektiven der Wissenschaft" Deutsche Bank Research, No. 02-3, 2002 to download at http://www.dbresearch.de/PROD/DBR_INTERNET_DE-PROD/PROD0000000000042525.pdf

127 Deutsch, Klaus "Research Notes in Economic & Statistics / Corporate Governance in Deutschland - Perspektiven der Wissenschaft"Deutsche Bank Research, No. 02-3, 2002 to download at http://www.dbresearch.de/PROD/DBR_INTERNET_DE-PROD/PROD0000000000042525.pdf at p.4

128 OECD „Institutional Investors - Statistical Yearbook 2001" to download at http://cs4hq.oecd.org/oecd/eng/TableViewer/wdsview/dispviewp.asp; also in Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance", Baden-Baden 1999 at p.29

Japan	2.427,9	3.154,7	3.644,8
United Kingdom	1.116,8	2.226,9	2.743,3
France	655,7	1.263,2	1.701,3
Germany	599,0	1.201,9	1.478,4
Netherlands	378,3	667,8	722,3
Total	12.053,4	24.382,0	29.547,8

This is derived not only from an increase in the countries with a traditionally large liquid financial market like the US, Japan, the UK and Canada[129] but also due to increased investment of this investor group in other strong economies like Germany, France and the Netherlands.

Although there is no generally acknowledged definition of the concept of the institutional investor[130], a number of useful characterisations are found in the literature[131]. Most authors define institutional investors according to three important features[132]. These include: that institutional investors are independent juristic persons; that they pursue a business purpose - investment and administration of outside assets by professional employees while ensuring satisfactory returns; and that their invested capital is above average and therefore has an essential influence on market trends. Hence, private insurances, pension funds and investment trusts can be included in this category. According to these traits, other organisations holding investments, such as statutory bodies, banks or trading companies, are not institutional investors[133].
With regard to Kapitalanlagegesellschaften (German investment funds) it should be stated that in Germany their interest is limited by the law (§ 60 s.4 s.1 InvG). The Kapitalanlagegesellschaft is allowed to invest only five percent of its special assets in securities of the same issuer. Consequently, a Kapitalanlagegesellschaft will always be a minority shareholder and cannot take over a company.

Having stated these definitions, it should be highlighted that a difference in the investment interests within the group of institutional investors becomes obvious. This is

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129 Newman, Peter/Milgate, Murray/Eatwell, John „The New Palgrave Dictionary of Money and Finance" London and New York, 1992 at Volume 2 "Institutional Investors"

130 Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance", Baden-Baden 1999 at p. 27

131 Tuerks, Robin A. "Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.27; Baums, Theodor/Fraune, Christian "Institutionelle Anleger und Publikumsgesellschaft: Eine empirische Untersuchung", Die Aktiengesellschaft 1995 at p. 97 ff; Kyrer, Alfred "Wirtschaftslexikon" 4th Edition Munich 2001 at p.273 "Institutionelle Anleger"

132 Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance", Baden-Baden 1999 at p. 27; Schiereck, Dirk „Institutionelle Investoren: Überlegungen zur Begriffsbestimmung bzw. -abgrenzung" in Sparkasse Volume 109, 8th Issue, 1992 p.393-394 at p.393; Newman, Peter/Milgate, Murray/Eatwell, John „The New Palgrave Dictionary of Money and Finance" London and New York, 1992 at Volume 2 "Institutional Investors"

133 Newman, Peter/Milgate, Murray/Eatwell, John „The New Palgrave Dictionary of Money and Finance" London and New York, 1992 at Volume 2 "institutional investors"

especially noticeable when comparing the pension funds with the investment trusts. On one side the investment trusts tend to pursue short-term rather than long-term profit maximisation[134]. Their objective is to strive for the best shareholder value, which allows them to sell their shares if problems lie ahead for the company, rather than to take initiatives via the company's management to correct the problems. As it can be seen in figures 10, 11 and 16 the safeguarding of the Kapitalanlagegesellschaft's interest is primarily exercised by voting. The interest in other corporate governance issues is more distinguished.

Figure 10: Role of German Institutional Investors as Shareholder[135]

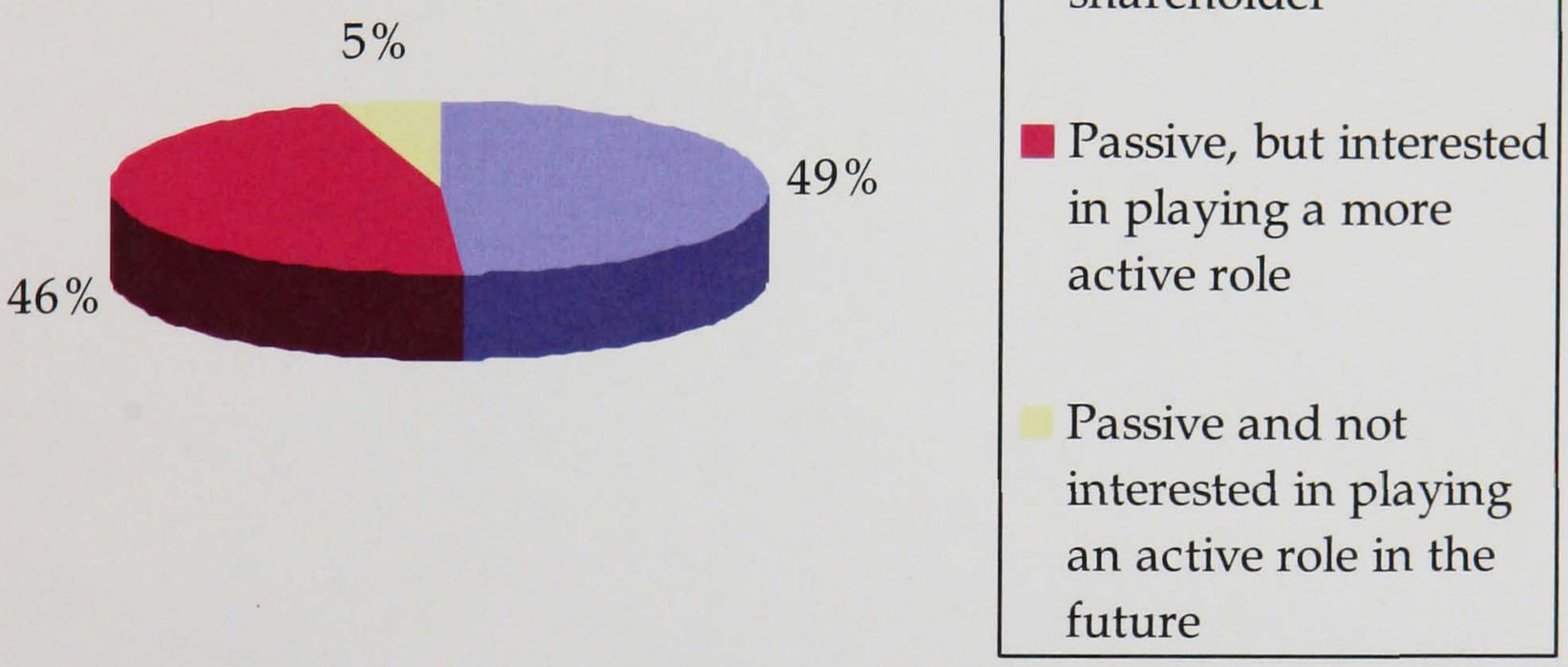
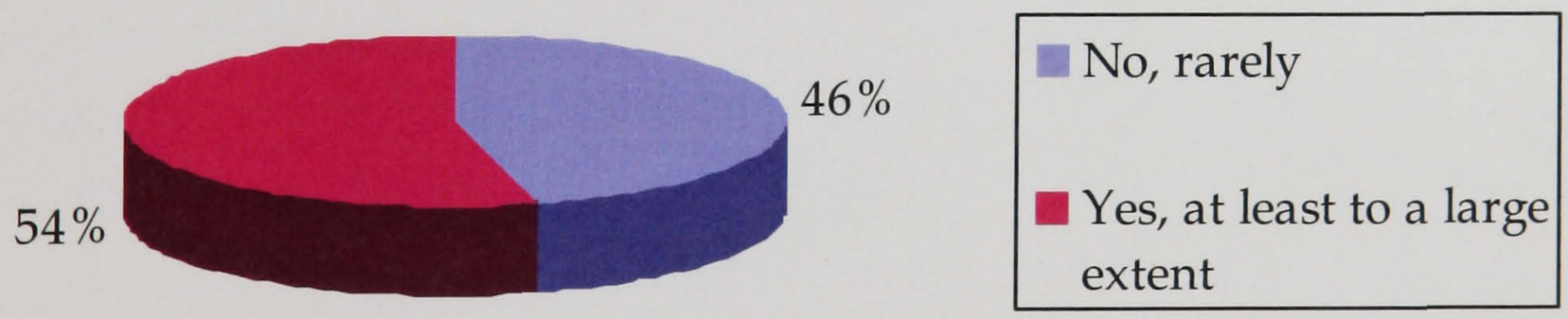


Figure 11: German Institutional Investors on Safeguarding their Voting Rights[136]



Having said that, it should be emphasised that although an increased interest by institutional investors in corporate governance is recognisable, their engagement (as the capital presence in the AGMs indicates) might still be improvable.

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134 Steiger, Maxin „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance", Baden-Baden 1999 at p. 53-57

135 Survey of the DSW – Deutsche Schutzvereinigung für Wertpapierbesitz among German Kapitalanlagegesellschaften, 2004 to download at www.dsw-info.de/DSW-Fondsumfrage.442.0.html#698

136 Survey of the DSW – Deutsche Schutzvereinigung für Wertpapierbesitz among German Kapitalanlagegesellschaften, 2004 to download at www.dsw-info.de/DSW-Fondsumfrage.442.0.html#698

On the opposite side there are the pension funds. They serve as organisations administering pensions of employees of one or several companies, employees of the public sector and other contributory members[137]. As they play a major part in the old-age pension scheme, they are facing a dilemma. While trying to maximise profits for the fund, they have to consider their investors, who are often stakeholders in the companies used for investment. Thus, striving for the best shareholder value cannot be the only interest of the pension fund. Their dilemma is that they need to look after the interests of their investors, while the long-term adjustment of contributions forces them to pursue medium- to long-term profit maximisation[138]. The number of proposals made during general meetings by the internationally operating pension funds supports this thesis[139].

It should be added that in Germany, pension funds mostly outsource asset management to investment companies[140]. Therefore they generally formulate guidelines and rules for the investment in order to safeguard their voting right and maintain compliance with the German Corporate Governance Code.

To draw a conclusion with regard to the concept of institutional investors, although investment trusts and pension funds are both included in this group, each one pursues different ways and time frames to maximise its profits. Taking this into account, a cautious approach is necessary when discussing the concept of institutional investors.

5.1.3. The Corporation as an Investor and the Issue of Crossholdings

The issue of the corporation as an investor becomes quite complex. On the one hand it may well be that the company only invested in another company for strategic reasons. Such motives can include:

- Creation and usage of synergies
- Completion of the range of products
- Building up presence in another market
- Control the pricing of ancillary industries

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137 Newman, Peter/Milgate, Murray/Eatwell, John „The New Palgrave Dictionary of Money and Finance" London and New York, 1992 at Volume 3 "Pension Funds"

138 Newman, Peter/Milgate, Murray/Eatwell, John „The New Palgrave Dictionary of Money and Finance" London and New York, 1992 at Volume 2 "Institutional Investors"

139 Good overview at Council of Institutional Investors: http://app.cii.org/mainpage.htm; California Public Employees' Retirement System: http://www.calpers-governance.org/alert/proxy/Item10i.asp; Florida State Board of Administration: http://www.fsba.state.fl.us/Investment.asp?FormMode=Call&LinkType=Combo&ID=13&Section=5

140 e.g. VBL -Versorgungsanstalt des Bundes und der Länder (Pensionfund of the Federal Government and the Laender) to Universal Investment, IBM Pensionfund also to Invesco, Metallrente (Belongs to the Trade Union) to dit/ADAM. An exception is Siemens Kapitalanlagegesellschaft who has the asset management in-house.

On the other hand, especially in Germany, crossholdings of stock corporations are still very popular (Compare with Figure 12 below). Only 27 of the 100 biggest German corporations are widely held[141].

The effect of these crossholdings on Corporate Governance and Shareholder Engagement in Germany has been subject to discussion and criticism. The intrinsic danger of this system is that corporate governance is almost exclusively based on the board-rooms and hardly on the general meeting.

Höpner[142] concludes that different interests for breaking up crossholdings exist: in the view of neoclassical thinkers, crossholdings are micro-economical inefficiencies. The Social Democrats criticise interweaving between corporations, because of the concentration of economical power. Höpner ads that interweaved corporations are not reactionary with regard to profitability and their behaviour towards the internationalisation of shareholders. When the company's ownership structure is opened towards corporate governing then these corporations will protect themselves from hostile takeovers by increased shareholder value strategies.

Whether crossholdings prevent profitability and internationalisation still needs to be proved, but in any case they hinder corporate governance. The danger that the corporations only look for each others interest is immanent. This assumption is supported by the finding of Carleton, Nelson, Weisbach that insider-controlled firms are less concerned about their reputation with shareholders[143].

The "exchange" of supervisory board members is certainly one symptom of the Deutschland AG, within which everybody knows and supports each other. Outside investors are heavily underrepresented and thus the insight from this angle is limited. Constructive criticism from this side could quickly be ignored. For these investors this is almost comparable with an exclusion from corporate control.

In addition to this the Deutschland AG represents an enormous lobby group, which could influence the development of German Company Law. Furthermore, crossholdings also have the effect that takeovers become extremely difficult, if not impossible[144]. Potential predators face a concentrated interest, which could easily block their efforts. The alternative is to aim for (an agreed) merger. Here again they have to

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141 Höpner, Martin„Unternehmensverflechtung im Zwielicht: Hans Eichels Plan zur Auflösung der Deutschland AG" Max-Planck-Institut für Gesellschaftsforschung 2000 to download at www.mpi-fg-koeln.mpg.de/sysbez/downloads/martin-Eichel.pdf at p.18f

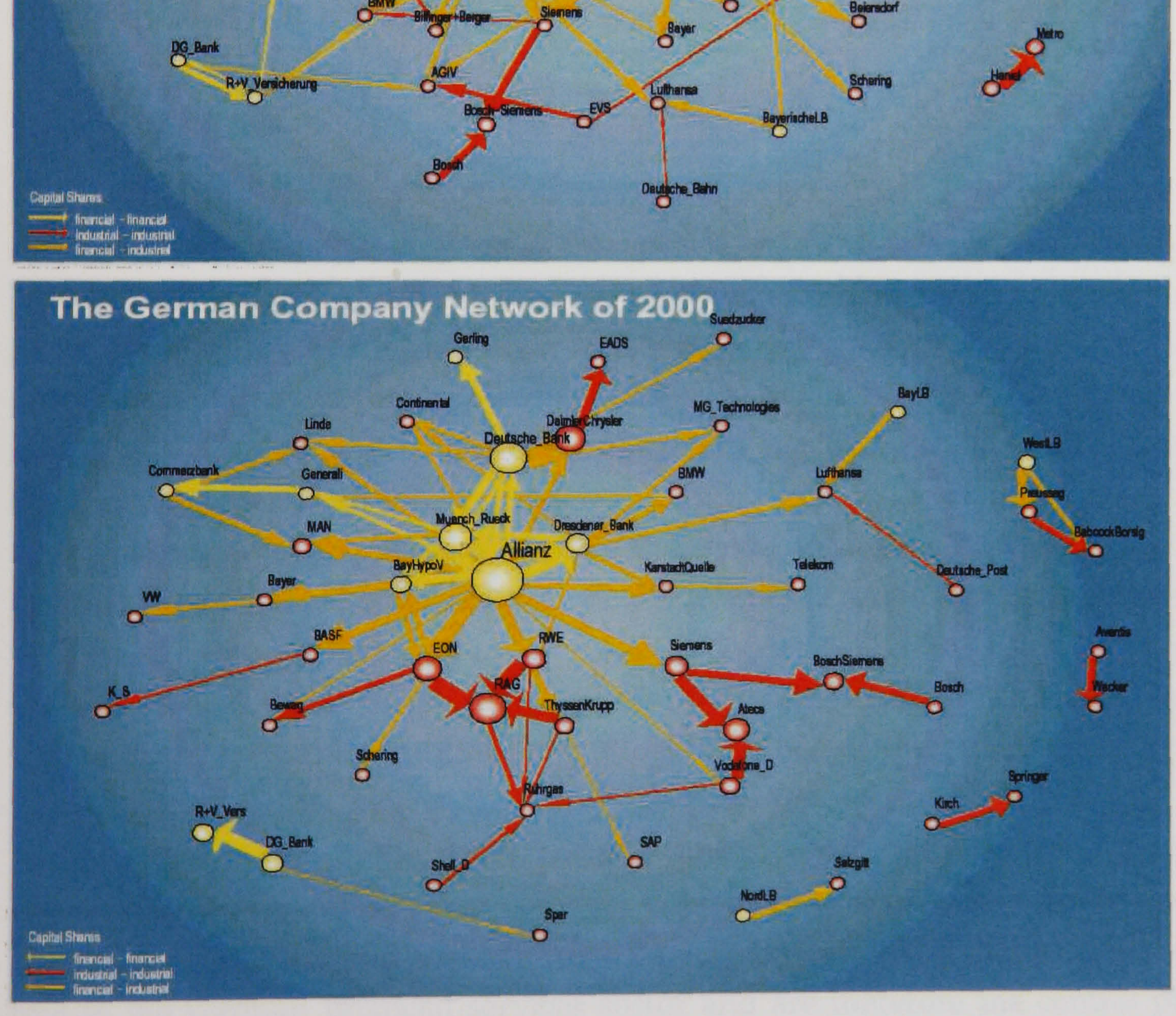
142 Höpner, Martin„Unternehmensverflechtung im Zwielicht: Hans Eichels Plan zur Auflösung der Deutschland AG"Max-Planck-Institut für Gesellschaftsforschung 2000 to download at www.mpi-fg-koeln.mpg.de/sysbez/downloads/martin-Eichel.pdf

143 CARLETON, Willard T. / NELSON, James M. / WEISBACH, Michael S. „The Influence of Institutions on Corporate Governance through Private Negotiations: Evidence from TIAA-CREF" in The Journal of Finance, Vol. LIII, No. 4, August 1998 at p. 1335-1362 at p.1349

144 Höpner, Martin „Unternehmensverflechtung im Zwielicht: Hans Eichels Plan zur Auflösung der Deutschland AG" Max-Planck-Institut für Gesellschaftsforschung 2000 to download at www.mpi-fg-koeln.mpg.de/sysbez/downloads/martin-Eichel.pdf at p.3

convince the large blockholder, because the majority for a takeover is 75% (§ 65 s.1 s.1 UmwG). The result is that corporate governance suffers.
When looking at the nexus of crossholdings it is considerably difficult to answer the question: Who owns whom?

Figure 12: Crossholdings in Germany[145]



145 Höpner, Martin/Krempel, Lothar „The Politics of the German Company Network" Max-Planck-Institut für Gesellschaftsforschung Working Paper 03/9 September 2003 to download at http://www.mpi-fg-koeln.mpg.de/pu/workpap/wp03-9/wp03-9.html

Although the German legislator altered the taxation for the sale of corporate holdings by corporations in 2000 (§ 8b KStG - Körperschaftssteuergesetz (Corporation Tax Act)), in order to decartelise the governance-hindering crossholdings, not much has happened since. The reason for the stagnation is the still unconvincing performance of the stock market, the difficulty to find a suitable buyer and the remaining economic interest in the holding company. However, the hope remains that the sale of corporate holdings will commence soon so that corporate governance can also be based on the general meeting and not exclusively on board-rooms.

For the sake of completeness corporate holding companies should also be mentioned. Although they are not supposed to acquire stocks of listed companies, they have considerable influence in all other legal forms of corporations. To characterise corporate holding companies, it could be stated that their only business purpose is the acquisition, administration and alienation of shares in other companies by the allocation of capital resources. The big difference to Kapitalanlagegesellschaften is the fact that they are not allowed to invest in listed stock corporations as previously mentioned.

5.1.4. The Banks

In contrast to some other legal systems, German banks are entitled to have a share in other companies (banks and other enterprises)[146]. As it can be seen in Figure 8, this possibility has a considerable impact on the ownership structure of German companies. Even though the banks see their interest as an investment and do not pursue entrepreneurial aims, their influence could result in conflicts of interest and even concrete obstructions (e.g. share in competing companies, establishing relations of economical dependency)[147].

This statement is emphasised by the additional influence the banks have through granted credits, share ownership through dependent Kapitalanlagegesellschaften and proxies as part of their custody services (Chapter 6.4.2.1.2.). As it has been shown above, German stock corporations finance themselves largely by credits, which they receive from the banks. Additionally, most often one of their business entities is asset management, which means that they have an investment fund holding numerous voting rights in-house. Moreover, in their function as a custodian bank they also offer proxy voting services to their (private) clients. Here the latter usually provides the custodian bank with full discretionary power. Consequently, banks have a universal role in the German financial services sector and are therefore the central pillar of the German economy.

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146 Schmidt, Thomas „Macht der Banken" Friedrich Ebert Stiftung, Bonn 1995 at http://library.fes.de/fulltext/fo-wirtschaft/00366toc.htm at p.19

147 Schmidt, Thomas „Macht der Banken" Friedrich Ebert Stiftung, Bonn 1995 at http://library.fes.de/fulltext/fo-wirtschaft/00366toc.htm at p.20

Nevertheless, it has to be emphasised that over the last years their influence shows a downward trend. One reason is the breaking up of the crossholdings, as already mentioned. Additionally, the heavy criticism of their influence on German companies and the fact that the proxy voting service[148] is not at all profitable, also foster their retreat from board rooms. Increased legal requirements like separating working proposals for the general meeting from own business interests (§ 128 s.2 s.3 AktG), the disclosure of personnel, and business interests with the corporation (§ 128 s.2 s.6, 7 AktG) also reduce the influence of banks further.

5.1.5. The Private Shareholders

In Germany the number of private shareholders has increased considerably, particularly with the introduction of the "T-Aktie[149]" and the Initial Public Offering of the Deutsche Telekom in 1996[150]. Although private shareholding suffered during the corporate crisis in the early 2000's, it should be noted that nevertheless, it has become widely spread and is no longer considered an exotic form of saving[151].

Figure 13: Share of the Population in Germany (over 14 years) Owning Shares[152]

Number of shareholders	1988	1992	1994	1996	1997	1998	1999	2000	2001	2002	2003	1. hy. 2004
Shareholders with employee shares	2,3 %	2,5 %	2,4 %	2,2 %	2,3 %	2,6 %	2,5 %	2,5 %	2,3 %	2,3 %	2,1%	2,1%
Shareholders with other shares	4,9 %	4,2 %	4,4 %	4,2 %	4,4 %	5,1 %	5,9 %	8,0 %	7,4 %	6,3 %	6,5%	5,8%
Among them with employee shares and other shares	0,4 %	0,4 %	0,5 %	0,4 %	0,5 %	0,6 %	0,6 %	0,8 %	0,8 %	0,8 %	0,8 %	0,8 %
Only employee shares	1,9 %	2,1 %	1,9 %	1,8 %	1,8 %	2,0 %	1,9 %	1,7 %	1,5 %	1,5 %	1,3 %	1,3 %
Only other shares	4,5 %	3,9 %	3,9 %	3,8 %	3,9 %	4,5 %	5,3 %	7,2 %	6,6 %	5,5 %	5,7 %	5,0 %
Total shareholders	6,8 %	6,4 %	6,3 %	6,0 %	6,2 %	7,1 %	7,8 %	9,7 %	8,9 %	7,8 %	7,8%	7,1%

Number of shareholders via an investment fund (fundholders)					1997	1998	1999	2000	2001	2002	2003	1. hy. 2004
Owner of equity funds					2,8 %	3,9 %	5,6 %	10,3%	11,1%	9,4 %	8,1%	8,2%
Owner of mixed funds					1,1 %	1,5 %	2,4 %	4,3%	5,8%	5,8 %	5,9%	5,4%

148 Volksbanken (cooperative banks) and Sparkassen Group (savings banks) have given up their proxy voting service in 2002. Source: (among other) DSW - Deutsche Schutzvereinigung für Wertpapierbesitz e.V. - Press Conference „Hauptversammlungsthemen 2003" 26.03.2003 to download at http://www.dsw-info.de/Hauptversammlungsthemen_2003.238.0.html

149 Name used to market the Telekom share

150 Gordon, Jeffrey N. „Working Paper No.161" in Columbia Journal of European Law, Vol. 5, No. 219, Spring 1999 (Symposium Issue) or http://papers.ssrn.com/paper.taf?abstract_id=208508 , see appendix chart: Private Investors in Germany

151 However, private shareholding in Germany is still not comparable with the UK or the US as figure 8 shows.

152 Deutsches Aktieninstitut: DAI-Factbook, August 2004 at 08.3-Zahl-D

Among them owner of equity and mixed funds					0,3 %	0,4 %	0,6 %	1,5%	1,7%	1,8 %	1,3 %	1,2 %
Only equity funds					2,5 %	3,5 %	5,0 %	8,8%	9,4%	7,6 %	6,8 %	7,0 %
Only mixed funds					0,8 %	1,1 %	1,8 %	2,8%	4,1%	4,0 %	4,6 %	4,2 %
Total fundholders					3,6 %	5,0 %	7,4 %	13,1%	15,2%	13,4%	12,7%	12,4%

Number of shareholders and shareholders via an investment fund (fundholders)					**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**1. hy. 2004**
Shareholders					6,2%	7,1 %	7,8 %	9,7%	8,9%	7,8%	7,8%	7,1%
Fundholders					3,6 %	5,0 %	7,4 %	13,1%	15,2%	13,4%	12,7%	12,4%
Among them with shares and funds					0,9 %	1,4 %	2,3 %	4,3%	4,1%	3,2%	3,2%	3,1 %
Only Shares					5,3 %	5,7 %	5,5 %	5,4%	4,8%	4,6%	4,6%	4,0 %
Only Funds					2,7 %	3,6 %	5,1 %	8,8%	11,1%	10,2%	9,5%	9,3 %
Total shareholder and fundholders					8,9 %	10,7%	12,9%	18,5%	20,0%	18,0%	17,3%	16,4%

With the private shareholder it is recommended to distinguish between the small private shareholder and the large investor. The group of small private investors is characterised by a share of widely held stock, with an alleged emphasis on shareholder value. Meanwhile the large investor shows a considerably high interest in the company. In Germany he is quite often a majority shareholder, also called "Familien AG". Consequently, large investors have a regular influence in forming the will of the company[153]. In addition to that, their general target is medium- to long-term profit maximisation. This derives from the amount of the shares they hold. As it is almost impossible for them to sell them in a short time without risking a considerable decrease of the stock price, they are forced to take an active part in the company's corporate policy.

Nevertheless, the small private shareholder deserves some more consideration. Generally, his motive to buy shares is the expectation of high returns.

Unfortunately, the small private shareholder does not have the best reputation with regard to exercising his vote[154]. This is often the result of indifference to the company's information (including the general meeting) and to his low share of votes. However, quite often it is the small investor who points out deplorable states of affairs of the company.

153 Krumnow, Jürgen/Gramlich, Ludwig „Gabler Bank Lexikon" 12th Edition, Wiesbaden 1999 at p. 641 „Großaktionär"

154 Grabert, Frank „Stimmrechtsvertretung im Aktienrecht – ökonomische Bedeutung und rechtliche Problematik" Dissertation with the University of Hohenheim 1995 to download at http://ourworld.compuserve.com/homepages/mox/diplom.htm 1.1.1.2.1

In contrast to the large and small private shareholder stands the employee shareholder. His initiative to invest in shares derives from stock option plans of the corporation[155]. Although the statistics regarding this issue are not overly expressive at this time, it could be assumed that their influence in some companies is more than considerable[156], especially when considering the employee representatives on the supervisory board. Considering the fact that they are employees of the company, they are not only a determining factor for social issues within the company, but also a reliable partner for the management in a take-over contest. Due to a contractual obligation to hold the shares for one to five years, she or he is forced to pursue long-term profit maximisation.

5.1.6. Further Investors (State, Foundations, Associations)

As a result of the privatisation offensive, the influence of the state as a shareholder has decreased, and this is likely to continue[157]. Nonetheless, in some German companies the federal government is still the largest shareholder[158]. The state certainly acts as a stabilising factor, but its own voting behaviour is often incomprehensible to others as they try to do the split between shareholder value and responsibility for the stakeholders. Hence, it is sometimes questionable whether the state is capable of taking an active role in the governance of a company[159]. The difficulty for the state is being able to distinguish between its role as a major shareholder and its role as a legislator. A state usually prefers to remain cautiously passive and err to avoid accusations of pursuing a company unfriendly economic policy.

It is also important to mention the existence of foundations[160] and associations[161] as shareholders. In accordance with their nature, foundations are closely related to corporate shareholders. However, it should be kept in mind that, in contrast to stock corporations, their relatively large capital resources are not based on stocks. Therefore if they intend to takeover a stock corporation they have to do it by cash payment rather than offering own stocks.

The group of associations could be defined as a union of small private shareholders who are pursuing common investment for common gain[162]. These associations of small

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155 Krumnow, Jürgen/Gramlich, Ludwig „Gabler Bank Lexikon" 12th Edition, Wiesbaden 1999 at p.1222 „Stock Option Plan"

156 see Figure 29: Shareholder Structure of Selected Stock Corporations 2004

157 see Figure 29: Shareholder Structure of Selected Stock Corporations 2004

158 e.g. Deutsche Telekom: 26% plus Kreditanstalt für Wiederaufbau 17%, Deutsche Post: 20% plus Kreditanstalt für Wiederaufbau 42,6%, Volkswagen: State of Lower Saxony owns 13,7%

159 Handelsblatt 20.03.02 „Eine Milliarde weniger für T-Aktionäre" - The German Ministry of Finance said that the decision to cutback the dividend by more than 40 % is "autonomous entrepreneurial" and that, therefore, no interference is planned. In the meantime the remuneration for the management board rose by 90 %

160 e.g. private foundations: Bertelsmann, Lidl or foundations under public law: savings banks, regional banks

161 e.g. investment clubs

162 Krumnow, Jürgen/Gramlich, Ludwig „Gabler Bank Lexikon" 12th Edition, Wiesbaden 1999 at p.742 „Investmentclub"

private shareholders, which could also be defined as investment clubs, should not be confused with shareholder associations like the Deutsche Schutzvereinigung für Wertpapierbesitz e.V. (DSW) or the Schutzvereinigung der Kapitalanleger e.V. (SDK). The objective of the latter is to protect the interests of small private investors.

The last group of shareholders to consider are foreign investors. However, they must be seen in the context of "globalisation", which is discussed in the next paragraph.

5.2. Globalisation and its Impact on Corporate Germany

Former German Chancellor Helmut Schmidt described the concept of globalisation as the "whip word" of these years. He argues that there are hardly any sensible definitions of the concept of globalisation. Most definitions are interest-motivated or political[163]. Therefore it is almost impossible to choose a politically "correct" definition. According to the probably innocuous Brockhaus encyclopaedia[164], globalisation is a term for the emergence of worldwide financial markets of securities, money and foreign exchange trading, as well as for loans, furthered by new information and communication technologies and innovations on the financial markets. Additionally, globalisation describes the increased competition of corporations on world markets.

The processes of globalisation have drawn a completely new landscape of shareholders; they have become more and more international. Foreign capital plays an increasingly important role in the global financial markets. In 2001 the share of foreign investors in Germany was 19,9 %[165] (DAX had a quote of 34%). Although this number is increasing it is compared to other countries (e.g. UK 32.4%, France 36.5%, Finland 73.6%[166]) still considerably low.
Anyhow, some of the renowned German stock corporations, like Deutsche Bank or Siemens, already show about fifty percent or more in foreign capital. As already mentioned above, this increase of foreign capital most probably resulted in the decrease of capital present at German AGMs. Additionally the increased investment by foreign capital also helped to break up cross-holding in Germany. The realisation that a cutting off by listed German companies against foreign investors will not benefit their long-term development led to the shift in thinking.

163 Schmidt, Helmut in „Globalisierung - Politische, ökonomische und kulturelle Herausforderungen" DVA, Stuttgart 1998 at p.7

164 Brockhaus Enzyklopädie 19th edition, Volume 8, Mannheim 1989 „Globalisierung" at p.597

165 European Social Investment Forum „Active Share ownership in Europe - 2006 European Handbook" to download at http://www.eurosif.org/content/download/355/2519/version/1/file/eurosif-ActiveShareOshipEurope2006.pdf at p.18

166 European Social Investment Forum „Active Share ownership in Europe - 2006 European Handbook" to download at http://www.eurosif.org/content/download/355/2519/version/1/file/eurosif-ActiveShareOshipEurope2006.pdf at p.18

Another welcome consequence of this development will be an increasing internationalisation of the boards. Especially the supervisory boards as the shareholders' body will take on a different complexion. Nowadays it has become normal that foreign shareholders are also represented on the board. The representation of employees in the supervisory board will certainly become an issue. Due to the fact that most stock corporations are global players and have facilities abroad, a discussion about representation of these foreign employees on German supervisory boards is certainly justified.

Besides supervisory boards, management boards also reflect the ongoing processes of globalisation, taking the Deutsche Bank (two out of six members including the CEO are not German) or the Deutsche Börse (again - two out of six members including the CEO are not German) as examples. Mergers and acquisitions also foster the internationalisation of stock corporations.

However, it also needs to be pointed out that the globalisation of German companies could result in strange effects. A good example of such effects is the rumour of a relocation of the Deutsche Bank headquarters from Frankfurt to London.

A concomitant of the ongoing globalisation of German corporations was an increasing intervention of politics into corporate decision making, which most often had a populist and protectionist background rather than an understandable economic one. Examples for this criticism are numerous: the interference in the bankruptcy of Philip Holzmann, the "locust debate", the Mannesmann case, almost permanently Deutsche Bank and more.

As we shall see in due course[167], in order to maintain the flow of foreign capital and to encourage foreign investors, the German legislator had to encounter this changing environment by providing solutions reflecting the ongoing globalisation of investors. The necessity to overcome deficits in the cross border information flow and in communication problems (e.g. language, shareholder identification) had the positive consequence that Germany tried to harmonise its Company Law system with international standards and also started to deregulate it. Good examples in this respect include the introduction of a record date, electronic proxy voting or the corporate governance code.

5.3. Types of Shares

Besides the identity of shareholders, understanding the different types of shares issued is also crucial here.

According to § 10 s.1 AktG stock corporations are generally free to choose whether they issue registered or bearer shares. This norm is complemented by §23 s.3 No.5 AktG.

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167 See Chapter 8. - The Legilator's Activity in Stock Corporation Law

According to this clause, the company has to specify in the articles of association the type of shares it will issue. It is also possible for the company to choose a split between bearer and registered shares[168].

5.3.1. Bearer Shares

The issuing of bearer shares is a particular trait of German corporations. As the name indicates, the ownership is transferred simply through the change of possession. Thus, the bearer is entitled to carry out the rights accompanying the ownership of the share (e.g. share lending or transfer of ownership by way of security). The evidence for the shareholder is given by the proof of deposit[169]. Therefore the great advantage of the bearer share is that it allows free and easy purchase and sale.

The great influence of the banks in Germany probably derives from the widely spread bearer share. On the one side, as corporations issuing bearer shares do not know their investors, contact is mediated via the custodian bank. On the other side shareholders often elect to leave their voting decision with the bank. This position as an almost unavoidable intermediate with the bearer share has allowed the custodian banks to become an important factor in forming an opinion of corporate decision making. Therefore the suggestion that any important decision by the company has to have the banks' blessing has much substance.

An additional problem that occurs is the personal distance between the company and its shareholder. In contrast to registered shares, this makes the bearer share unsuitable for investor relations. The company is only able to address the issue of investor interests in quite a general way, which might not meet the information request of the shareholder. This could put the latter in a position where he is more prepared to sell his shares compared to a registered shareholder, where the information request is more likely to be met and more attention is provided to the investor.

5.3.2. Registered Shares

5.3.2.1. Rediscovering the Registered Share

More remarkable than the bearer share is the registered share. To understand its recent movement within the German Stock Corporation Act, it is certainly necessary to gain an

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168 Hoffmann-Becking, Michael "Münchner Handbuch des Gesellschaftsrecht - Band 4 Aktiengesellschaft" 2nd Edition Munich 1999 § 13 No.1 (Hoffmann-Becking)

169 Noack, Ulrich „Entwicklungen im Aktienrecht 1999/2000" at IV. 1. a), to download at http://www.jura.uni-duesseldorf.de/dozenten/noack/texte/noack/entwicklung.htm

overview of the implications of the registered share. The conveyance of property using registered shares is more complicated than is the case with bearer shares.
The registered share is mainly regulated in § 67 AktG. According to this paragraph, the name, date of birth, and address of the holder shall be entered in the stock corporation's register as well as the number or serial number of the shares he is holding. Legal persons, companies and similar entities are registered with name, headquarters and address, including the address of a proxy agent or an e-mail address[170].

Only the registered person will be treated as a shareholder. So the presentation of the share, according to § 68 III S.2 AktG, will become irrelevant. The simple proof of transition, e.g. in the case of share lending, will be sufficient (although at least non-listed companies may have the right to refuse to register a transfer). With regard to data processing this is a great relief. If a registered share is transferred to another person, the stock corporation has to update its register. For the stock corporation, the registered person is seen irrevocably as the shareholder. However, this is not valid with regard to a third party. The bank, which might be registered as a shareholder, cannot claim any rights from the registration towards its custody client[171]. Due to § 128 I AktG the registered custodian bank shall promptly forward any information (pertinent to § 125 I AktG) to such shareholders.

When the first stock corporations were created 150 years ago registered shares were quite popular. However, it was not until the end of the 1990`s when the registered share was rediscovered by a number of stock corporations, as von Rosen and Seifert have noted[172]. The reasons for this turning point in favour of registered shares are manifold[173]. The registered share is perfect as a currency for takeovers and therefore allows shares of a company to be exchanged; the circulation of registered shares is worldwide, especially in the United States where registered shares are required for listing on the New York Stock Exchange (bearer shares, in contrast, would require an American-Depositary-Receipts-Programme[174]); the stock register enables counter-

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170 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz - NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf at § 67 I AktG

171 Spindler, Gerald „Internet und Corporate Governance - ein neuer virtueller (T)Raum?" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 3/2000 p. 420-445 at p.423

172 Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm at p.7

173 A number of authors share these reasons, although their emphasis differs: Merkt, Hanno "Die Geschichte der Namensaktie" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.63-96 at p.88ff; Seibert, Ulrich „Die gesetzliche Neuregelung" in Rüdiger von Rosen/Werner G. Seifert "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.11-45 at p. 12 f; Zschocke, Christian „The German Stock Corporation Act - Introductory Act to the Stock Corporation Act" Frankfurt am Main 3rd Edition 2001 at p.11

174 Definition by the International Corporate Governance Network at www.icgn.org
American Depositary Receipts (ADRs) are one of the most popular methods by which US investors gain exposure to foreign securities (For ADRs to be within the US pricing levels, they may represent more than one share of a foreign Issuer or a fraction of one share of a foreign Issuer). In comparison to owning foreign securities directly, ADRs provide benefits to US investors who wish to own foreign securities, including easy transfer of shares, payment of dividends in US

measures to hostile takeovers to work more successfully; a deciding factor was also that companies could enhance their investor relations using registered shares; and finally, the global pressure to harmonise company, stock market and capital market laws led to the proliferation of registered shares.

However, the spreading of the registered share should not be overestimated. Although a number of the most important German issuers (Deutsche Bank, Allianz, Epcos, Deutsche Telekom, Deutsche Post and others; global share: Daimler Chrysler) have made a decision in favour of the registered share, the number of such issuers is still limited to only about 6% of the 829 (in Dec. 2003) listed and 10% of all stock corporations (8.622 in Dec. 2003)[175]. In addition to that, it seems that the early enthusiasm for the registered share has disappeared. This is to a certain extent understandable, as the expected rise in capital presence did not take place[176].

The switch to registered shares is unattractive for other reasons, particularly for small corporations. Most of all, companies fear the high assignment costs, and quite often for good reasons. Especially in companies with one or more large shareholders it is certainly questionable whether the benefits of registered shares will outweigh the costs of an assignment. However, if the corporation has chosen to introduce registered shares, it is possible to keep administration costs to a similar amount as when using bearer shares[177], through the collective deposit of securities.

5.3.2.2. Data Pool: Register

It is important to mention that an external company can carry out the conduct of the stock corporation's register. In contrast to the Anglo-American countries, where the transparency of registers is not very advanced, German registers hold far more information and hence make them quite attractive as a data pool for all kinds of purposes. This derives from the fact that compared to the German registered share the American is at a considerable disadvantage, as the broker has an almost universal position. In contrast to the German system, where the beneficial owner is stated in the registers (in most cases), the US shareholder is only registered within the accounts of his

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dollars, and facilitation of compliance with foreign investment restrictions and requirements. Similarly, ADRs and other forms of depositary receipts also are attractive vehicles for many non-US investors for investments in emerging markets. Non-US investors of ADRs appreciate the greater security and liquidity that these instruments offer over direct investment in certain markets.

→A more detailed definition could be found in the Appendix under Definitions

175 Deutsche Börse Group „Factbook 2003" to download at http://www3.deutsche-boerse.com/INTERNET/IP/ip_stats.nsf/(KIR+Factbook+Kassamarkt)/BD587F972E5DF758C1256E850045DAEB/$FILE/Factbook_2003_d.pdf?OpenElement at Figure 1.1.2

176 see Figure 6: Presence at DAX 30 AGMs (1998-2005)

177 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz - NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf at Allgemeine Begründung

broker. A continuing registration does not exist, which can lead to difficulties with the evidence of property[178]. Such difficulties include problems in tracking the beneficial owner (e.g. in the case of takeover offers), and also in the case of disputes about the ownership of shares, say between the broker and his investor.

Another issue with the German registered share is that of data protection. Before the NaStraG[179] in 2001 each investor was entitled to get information about other shareholders from the register. Moreover, a registered shareholder was not supposed to object his registration. Hence, every other shareholder could gain any information regarding any of his fellow investors from the register[180]. This lack of privacy was solved by allowing the entitled shareholder to examine only his own registration, either in person or, if it has been made possible, via an on-line inquiry[181].

A further issue is the company's use of data gained from the stock register. In forming the bill, the legislator made clear that § 67 s.5 AktG entitles the company to utilise all data of the shareholder for earmarked purposes such as all kinds of marketing of the corporation's products. The legislator is of the opinion that the shareholder has an alleged interest in what the company is doing. If he is not interested in any material of the company, he can inform them of his opinion[182]. Weber points out that the commercial economy criticised this approach[183]. Although the use of gained data for advertisement is not outlawed, companies should choose a low-key approach to take account of the fact that a shareholder is not comparable to an interested customer. Heidorn, Schmidt and Seiler express their opinions that due to the company's knowledge of the name, gender, address, age and the number or registration number of the registered shares, it is possible to construct an expressive profile of their shareholders[184]. The gained data could undoubtedly be utilised by the company to develop profiles on the movement and investments of shareholders.

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178 Wunderlich, Michael/Labermeier, Alexander „Rechtliche Behandlung, Übertragung und Börsenhandel von Namensaktien in den USA" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.143-175 at p.173

179 NaStraG - Gesetz zur Namensaktie und zur Erleichterung der Stimmrechtsausübung 2001 (Law on Registered Shares and Simplified Rules for the Exercise of Voting Rights)

180 Dammann, Ulrich/Kummer, Tanja – Bundesbeauftragter für Datenschutz „Namensaktie und Datenschutz" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm at 45-62 at p.48ff

181 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz – NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf at § 67 Abs.6 AktG

182 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz – NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf at § 67 Abs.6 AktG

183 Weber, Martin „Der Eintritt des Aktienrechts in das Zeitalter der elektronischen Medien - Das NaStraG in seiner verabschiedeten Fassung" in Neue Zeitschrift für Gesellschaftsrecht (NZG) 8/2001 p. 337-346 at p. 340

184 Heidorn, Thomas/Schmidt, Peter/Seiler, Stefan „Neue Möglichkeiten durch die Namensaktie" Work Report No. 23 Hochschule für Bankwirtschaft Frankfurt 2000, also Spindler, Gerald „Internet und Corporate Governance – ein neuer virtueller (T)Raum?" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 3/2000 p.428

However, it is not in the issuer's interests to distribute information amongst its registered shareholders unequally. An example of violating the equal treatment of shareholders principle would be the notification of a majority shareholder that the period to sign for new shares is about to expire, whilst leaving the remaining shareholders unaware of this message[185]. Allowances could be made to the extent of "special announcements for marketing purposes"[186] as Noack calls them, with the knowledge that not being informed of company matters could be a shareholder's basis for compensation claims.

A crucial question is whether the register's information could be used to detect when a takeover is about to take place[187] and consequently, to allow the firm to engage counter measures against a shareholder before his takeover action is implemented. Hommelhoff and Teichmann[188] support the opinion that this usage is not possible, as counter measures against a takeover bid are not a specific task of the company and hence, are not covered by § 67 s.6 s.3 AktG. Furthermore, the shareholders are obliged to disclose their data in the register, this data must not been used against them. Finally, Hommelhoff and Teichmann refer rightly to the share disclosure requirements of the Wertpapierhandelsgesetz - WpHG (Securities Trade Act): Providing this is a shareholder's only data source it is not understandable why a corporation should receive special treatment.

In conclusion the obvious advantage of the registered share is that it provides greater transparency of the corporations' business (registration, disclosure of accounts, ad hoc disclosure, reports in the event of specific occurrences within the company). The registered share improves the information flow between the company and its investors considerably. This a step in the direction of the position taken by the US Securities and Exchange Commission (SEC), which has long applied the principle of "disclosure, again disclosure and yet more disclosure" in the search for transparency within capital markets. Although some authors generally see the United States as still further

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185 Hommelhoff, Peter/Teichmann, Christoph „Namensaktie, Neue Medien, und Nachgründung - aktuelle Entwicklungslinien im Aktienrecht" in Dörner, Dietrich/Menold, Dieter/Pfitzer, Norbert/Oser, Peter „Reform des Aktienrechts, der Rechnungslegung und der Prüfung" 2nd Edition Stuttgart 2003 at p.103-134 at p. 112

186 Noack, Ulrich „Namensaktie und Aktienregister: Einsatz für Investor Relations und Produktmarketing" in Der Betrieb (DB) 2001 p.27-31 at p.28

187 With sceptisism on the further utilisation on gained data: Spindler, Gerald „Internet und Corporate Governance - ein neuer virtueller (T)Raum?" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 3/2000 p. 420-445 at p.426

188 Hommelhoff, Peter/Teichmann, Christoph „Namensaktie, Neue Medien, und Nachgründung - aktuelle Entwicklungslinien im Aktienrecht" in Dörner, Dietrich/Menold, Dieter/Pfitzer, Norbert/Oser, Peter „Reform des Aktienrechts, der Rechnungslegung und der Prüfung" 2nd Edition Stuttgart 2003 p.103-134 at p.113f

developed than the European Union[189] the fostering of the registered share is certainly a step towards greater transparency in the German market.

5.3.3. Preference Shares

According to § 139 s.1 AktG it is also possible to issue preference shares. They must be vested with an extra payable preference with the allocation of the profits. More important with regard to shareholder engagement is the possibility to exclude the voting right[190]. Such shares can only be issued up to half of the capital stock (§ 139 s.2 AktG). Hence, they are only a supplementation to the ordinary share. Their purpose is to make self-financing easier and to satisfy the interest of those investors who are only interested in yield and increase of substance[191].
In recent years the preference share has gained considerable importance[192], not only because of its financial possibilities but also as it is able to make takeovers difficult[193]. Especially because of this reason, the preference share has to be viewed critically, particularly as the share price displayed its own dynamic, which normally does not stand in relation to that of the ordinary share[194].

5.4. Implications of Modern Communication Forms

As we have noted already, the increasing popularity of investing in the stock market since the end of the 1990's, particular because of the introduction of the "T-Aktie" by the Deutsche Telekom in 1996[195], has had an impact on the environment of shareholder engagement. Additionally, the reform of the old-age pension scheme will also have a large impact upon the ownership of shares of German companies. These developments have demanded an increased applicability of modern communication forms, which changed the landscape of stock corporations as well. Noack[196] describes the implications of forms of modern communication on the German Stock Corporation Act:

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189 Noack, Ulrich „Moderne Kommunikationsformen vor den Toren des Unternehmensrechts" Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 3/1998, S. 592-616 and to download at http://www.jura.uni-duesseldorf.de/dozenten/noack/texte/noack/kommunik.htm at IV 1; Tuerks, Robin A. "Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.84

190 For special rights with the preference share see chapter 6.2.5.1. Voting Restrictions

191 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 139 No.2; Hopt, Klaus J./Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition Berlin 1999 at § 139 No.6 (Bezzenberger)

192 Hopt, Klaus J./Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition Berlin 1999 at § 139 No.7 (Bezzenberger)

193 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 139 No.3

194 The spread in the share price between the ordinary share and the preference share in a statistic by the bank Merck Finck & Co. of 1996 respectively 1997 → Hopt, Klaus J./Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition Berlin 1999 at § 139 footnote No.7(Bezzenberger) ranged from 0,7% with SAP to 72,2% with Dyckerhoff in 1996 and from -4,1% with SAP to 75,4% with SPAR in 1997

195 Gordon, Jeffrey N. „Working Paper No.161" in Columbia Journal of European Law, Vol. 5, No. 219, Spring 1999 (Symposium Issue) or download at http://papers.ssrn.com/paper.taf?abstract_id=208508 , see appendix chart: Private Investors in Germany

196 Noack, Ulrich „Moderne Kommunikationsformen vor den Toren des Unternehmensrechts" Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 3/1998, S. 592-616 and to download at http://www.jura.uni-duesseldorf.de/dozenten/noack/texte/noack/kommunik.htm at IV 1

Five hundred years ago paper printing was a modern form of communication; a hundred years ago telegraphy was invented; for fifty years the telephone has been in common use, and for ten years fax machines have been spread widely. These technical innovations simply have not had recognisable influence on stock corporations.
The increasing use of computer based online-systems has certainly not edged out more traditional forms of communication such as using the telephone, writing letters and using fax machines. Computer based systems are not even expected to make these forms of communication obsolete, but they have most certainly made a vital contribution to communication with innovations like E-mail, SWIFT, Internet, Intranet and computer based conferences via ISDN.

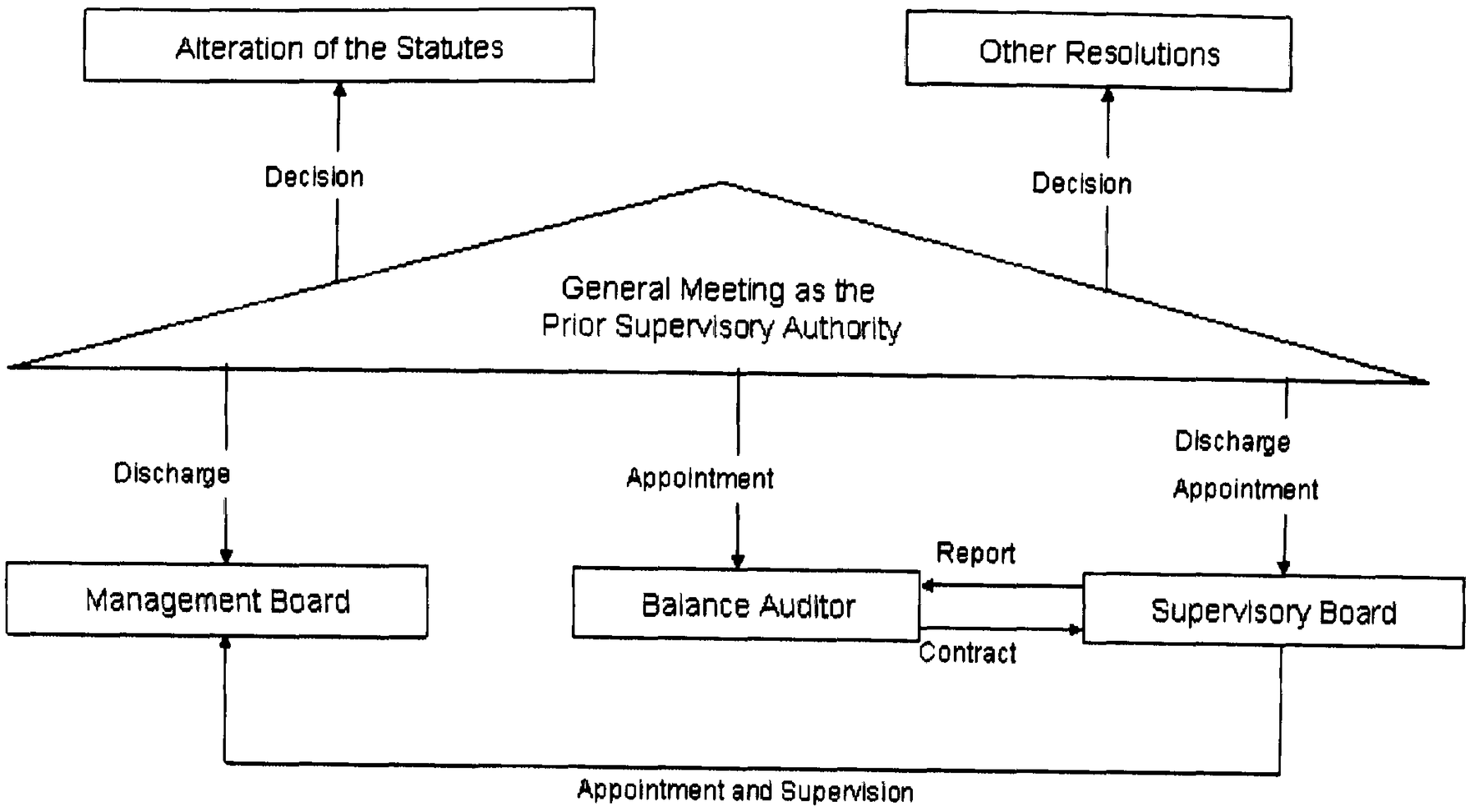
The need for reform was also emphasised by a number of stock corporations. Blue-chip stocks changed their shares from bearer equities into registered. Other companies, mostly in the former Neuer Markt sector, were issuing registered shares right from their initial public offering. For instance a traditional form of keeping the registers was, out of financial and organisational reasons, not in the interest of the market participants. The established Girosammelverwahrung (electronic keeping of registers) by the NaStraG provides a universally applicable keeping of the registers. Furthermore, electronic proxy voting or the electronic edition of the Bundesanzeiger (federal gazette) should also be mentioned at this point.
In addition to that, it had to be recognised that the Stock Corporation Act was not appropriate for the new economic situation. The technical and procedural conditions in the year of introduction (1965) on which the Stock Corporation Act was based have become outdated. Furthermore, the legislator had to recognise that the circle of shareholders was no longer manageable and predominantly national[197]. The growing request for information and an increased diversification of private and institutional shareholders considerably enhanced the requirements for distributing company data as well as the notice to the annual general meeting.
All these implications of modern communication forms improved the environment for shareholder engagement considerably and moreover, accelerated the reform of Company Law.

5.5. Purpose and Duty of the General Meeting

The central body for shareholder engagement is the general meeting. As it can be seen in Figure 14 , it carries a number of responsibilities.

197 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz - NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf

Figure 14: Responsibilities of the General Meeting[198]



The annual general meeting[199] serves two purposes. It is the platform on which the management informs and accounts to the shareholders and it is also the decision-making body of the shareholders[200]. It decides only in those cases explicitly stated in the law or in the articles of association (§ 119 s.1 AktG). The decisions primarily concern the control of the administration such as election of the supervisory board representatives; appointment of the balance auditors; discharge resolutions; appointment of special auditors; and resolutions for the prosecution of damage claims against members of the administration body. They also dispose to a certain extent over the basis of shareholders' investments (alteration of the articles of association, closing down of the corporation, structure-changing resolutions)[201].

In its "Gelatine[202]"as well as in the "Holzmüller[203]" - ruling the Bundesgerichtshof-BGH (Federal High Court)[204] laid down the decision competences of the general meeting. In both cases the court dealt with the question under which conditions the management needs to seek approval in the general meeting for structural changes of the company. The "Holzmüller" ruling (1982) approved that structural changes, which effect the codetermination and administration rights of the shareholders are binding externally, but could cause claim for damages or injuctive relief to the benefit of the shareholders. Hence, the management should seek approval in the general meeting.

198 Supplemented Draft – original in "Gabler Wirtschaftslexikon" 15th Edition Wiesbaden 2000 at p.654 – Corporate Governance

199 The number of special general meetings in Germany could be estimated as less than 1% of general meetings in total

200 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at p. 78

201 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at p. 78

202 „Gelatine" II ZR 155/02 in die Aktiengesellschaft 2004 p.384-389

203 „Holzmüller" II ZR 174/80 in die Aktiengesellschaft 1982 p.158-167

204 Hierarchy of German Civil Courts: Bundesgerichtshof – Oberlandesgericht – Landgericht - Amtsgericht

Unfortunately, the BGH renounced to define precise conditions for the structural changes. This legal gap was picked up by the "Gelatine" ruling (2004). Fuhrmann[205] explains the situation as follows: The legislator made the general meeting the leading institution of the stock corporation but it did not pass on all responsibilities to it as the general meeting does not provide the structural requirements to control the company with the necessary flexibility. More specifically, in "Gelatine" the court ruled that unwritten participation powers of the general meeting are only acceptable within narrow limits when measures of the management are affected:

Firstly, the measure needs to be a fundamental encroachment of member and property rights of the shareholders. In this respect Götze clarifies that the encroachment in its consequences must get close to an alteration of the statutes[206].

Secondly, a threshold value of far more than 50% of the company's assets must be exceeded.

Consequently, with this narrow definition the BGH strengthened the position of the management in contrast to that of the AGM.

As the stock corporation does not have a hierarchical constitutional body, the general meeting is not the supreme authority. Hence, equilibrium between the management board, the supervisory board and the general meeting is typical in corporate Germany[207]. This is an indication of the importance of shareholder engagement.

It should not be neglected that the existing order of the general meeting is readily questioned. The excessive use of some shareholder rights, like the petition right, made this body an overloaded gathering of investors, which serves "socialising" purposes (the meeting of old colleagues) and thus acts inefficiently.

In his standard work on the general meeting of the stock corporation, Butzke particularly criticised[208] three features. The high presence of shareholders in the general meeting (which often is in contrast to the capital presence), abuse of the petition right, which prolongs the meeting disproportionately and attempts by shareholders to make resolutions contestable.

Having provided a comprehensive view of the benefits and the wider environment of shareholder engagement, the following chapter will deal with the claimed hierarchy of shareholder engagement set out in Chapter 1.2.

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205 Fuhrmann, Lambertus „"Gelatine" und die Holzmüller-Doktrin: Ende einer juristischen Irrfahrt?" in Die Aktiengesellschaft 7th Edition 2004 p.339-342 at p.340

206 Götze, Cornelius „"Gelatine" statt „Holzmüller" - Zur Reichweite ungeschriebener Mitwirkungsbefugnisse der Hauptversammlung" in Neue Zeitschrift für Gesellschaftsrecht Vol.7 13/2004 p. 585-589 at p.586

207 Eisenhardt, Ulrich "Gesellschaftsrecht" 11th Edition, Munich 2003 at No.574

208 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.4ff

6. Chapter: The Legal Environment for the Hierarchy of Shareholder Engagement

As we have seen, shareholder engagement in Germany is still in a process of development. It is crucial that it is pursued most effectively, is in the interest of the company and its stakeholders, and does not infringe the law. In order to achieve this task a hierarchy of shareholder engagement was introduced in Chapter 1, which set out the framework of a sound shareholder engagement. Using an escalating order, this Chapter will now apply the hierarchy of shareholder engagement.

The fact that it is the right of the shareholder to have a say in company matters at the general meeting is quickly recognised when attending an AGM in Germany.
On the one hand, it is certainly an improvement for the corporate governance of a company, when a third institution other than the law and supervisory board, that is the shareholder meeting, supervises the performance of the management board. The general meeting has often urged management to change company policy and to improve shareholder value. Awkward questions are also capable of showing weaknesses within the enterprise.
On the other hand, the status of being a shareholder is frequently used to achieve personal aims at the expense of the company. An example within this context is the type of investor who tries to find an occasion in the general meeting to block a resolution through a suit in order to demand financial compensation from the company to withdraw the legal action[209].

6.1. Information Right

An essential condition for the shareholder to pursue a responsible engagement and thus make his contribution to good corporate governance, is the information right according to § 131 AktG[210]. Its purpose is to enable the shareholder to carry out his job as a member of the corporation in a responsible manner. Only broad knowledge about the

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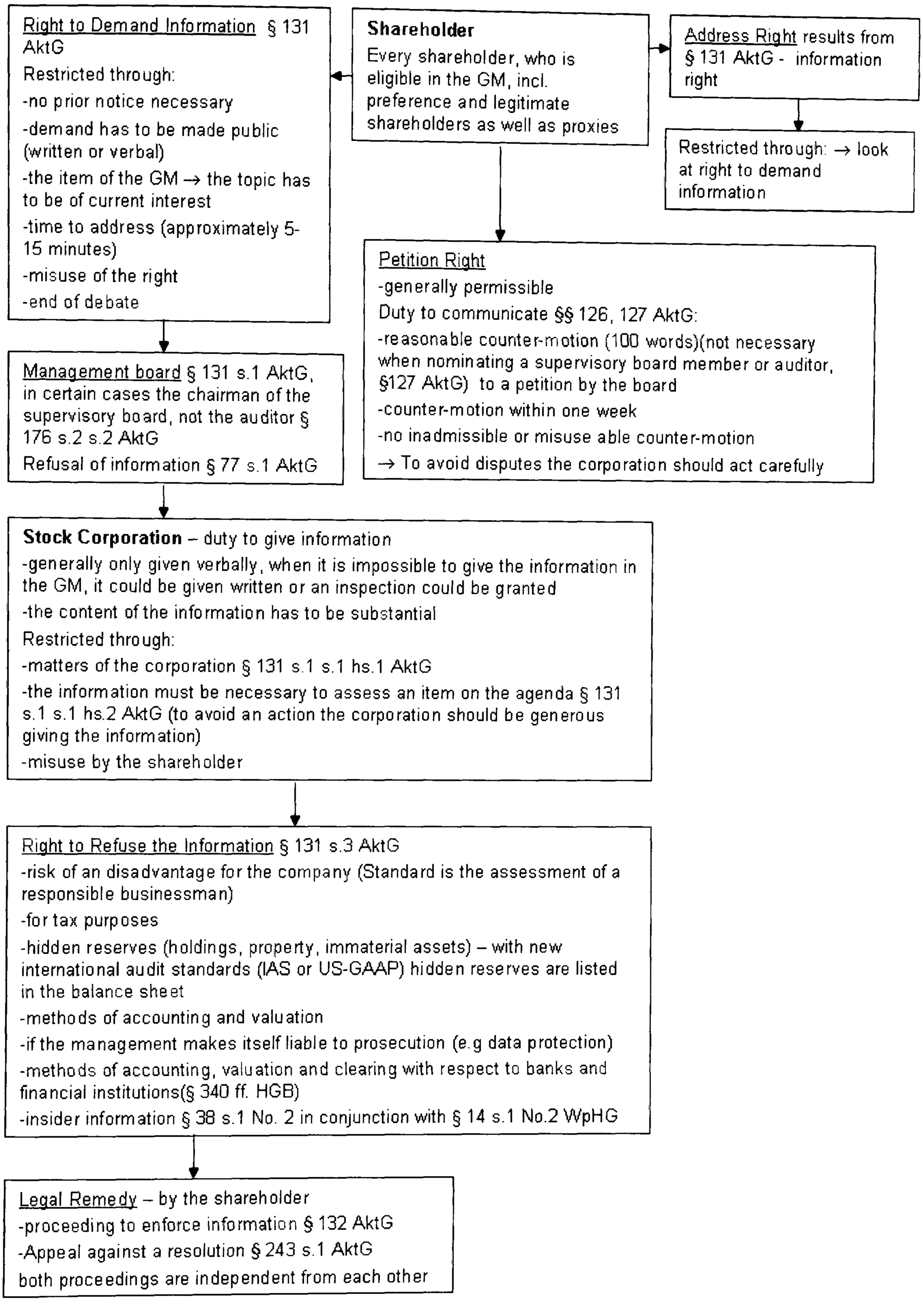
209 It remains to be seen, if the UMAG of 2004 is capable to stopp the abuse of the right to sue. For more information look at chapter 9.4. UMAG

210 § 131 s.1 AktG Upon request, each shareholder shall be provided with information at the general meeting by the management board on the stock corporations' affairs to the extent that such information is necessary for a proper evaluation of an item on the agenda. The duty to provide information shall also extend to the stock corporation's legal and business relationships with any affiliated company. If a stock corporation makes use of the simplified accounting procedure pursuant to § 266 s.1 s.3, § 276 or § 288 of the Commercial Code, at the general meeting on the annual statements, each shareholder may request that it be presented with the annual financial statements in the unabridged form in which the accounts would have been if such provisions had not been applied.
§ 131 s.2 AktG The information provided shall comply with the principles of conscientious and accurate accounting.
§ 131 s.3-s.5 AktG not primarily necessary to grasp the scope of the information right

company's affairs allows him to act in its interest. Hence, due to the position of the shareholder, this right is a priority for him to use his vote competently[211].
The diagram below provides a complete hierarchy of this information right from obtaining material to suing the company.

Figure 15: Information, Address and Petition Right in the General Meeting

211 Hopt, Klaus J./Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition Berlin 2001 at § 131 No. 7 (p.9) (Decher)



6.1.1. Collective Information

In § 121 s.3 and s.4 AktG the Stock Corporation Act provides that the company has to give notice to the shareholders as the general meeting approaches. Along with the

notice of the general meeting, additional information is distributed to the shareholders[212]. This information includes, but is not limited to:
-the agenda and items for resolution
-suggestions for resolutions including complementary explanations
-the annual settlement and eventually a consolidated settlement
-information with the loss of 50% or more, of the capital stock
-explanation of contracts and resolutions, which have to be approved by the general meeting
-reports in connection with structural measures, including reports of examination and other documents: e.g. report of a merger and report of a division

Butzke coined this kind of material "collective information"[213]. Its distribution by the company is not only requested by the law and necessary to avoid a flood of inquiries at the general meeting, but also to meet its duties towards investor relations. It is advisable for the company to take the quality of the information seriously as it is often a yardstick for the investor to stay with the company, or to trade his shares.
The concept of collective information could be defined as material that is relevant for the forming of an opinion on matters of the agenda. It is given out by the stock corporation with the aim to inform the broadest possible spectrum of shareholders. Depending on the cost, this could happen in a number of forms, primarily according to the requested legal security. Hence, the notice to the general meeting is published in the Bundesanzeiger and additionally, every shareholder receives an individual statement. Certainly, not every topic can be covered this way; too manifold are the interests of the different shareholder groups. While institutional and corporate investors, banks, certain shareholder associations and the majority of private shareholders are mostly satisfied with positive figures in the report, interest groups, in particular employees, tend to scrutinise the company as a whole. Quite often the chief executive officer has to answer questions about the employment policy with regard to dismissals, overtime, handicapped and women, or the company's attitude towards environmental matters and more. Hence, the collective information can only serve as a tool to limit the thirst for information in the general meeting.

It is essential to mention the duty of information with ad-hoc announcements according to § 15 WpHG. As per this paragraph, the management of a listed stock corporation has to issue facts immediately, which might influence the share price considerably. The ad-hoc announcements have to be published in at least one national deposit financial paper[214]. Unfortunately, especially in the former Neuer Markt Index numerous

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212 following: Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.230

213 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.230

214 Very useful on this Issue: Leis, Josef/Nowak, Eric „Ad-hoc Publizität nach § 15 WpHG" Stuttgart 2001

companies abused this provision to state share-price-influencing facts to market the performance of their company. By publishing whitewashed and exclusively positive information about the company, which were often not based on facts[215], they intended to increase their market value and thus raise the stock's price. In a number of cases the public prosecutor's office has made inquiries.

6.1.2. Entitled Person and Obligated Party

The information right is compelling for the company, meaning that every shareholder who is eligible to attend the general meeting, including his legitimate proxy and owners of preference shares with no vote or unit shares, are entitled to this right. The articles of association can neither restrict nor extend this right. Only outside the general meeting certain regulations in the articles of association are permissible[216]. Correspondingly, this is also valid for boards of control.
The obligated party is the stock corporation. The duty to inform is first of all carried out by the management board on behalf of the corporation[217]. This is true for information given by other departments, which the board also announces as its own communication. In other words, the board is the only institution to give out binding information.

6.1.3. Conferral of Information

Due to § 131 s.1 s.1 hs.1 AktG, the requested information has to be about matters of the corporation. Hüffer states in his comments that, everything referring to the stock corporation and its activity, including customer and supplier relations and the relationship with connected enterprises, can be subsumed under this point[218].

In general, the information is given verbally at the general meeting. Only when it is impossible to give the information in the set frame of time at the general meeting, may it be conferred in writing, or can inspection of the firm's books be granted to the shareholder. The content of the conferred information has to stand up to the principles of thorough and true accounting (Grundsätze einer gewissenhaften und getreuen Rechenschaft)[219]. Therefore the statements of the management board must be truthful, and the board cannot hold back important facts[220]. If a member of the board disguises

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215 e.g. EMTV, Kabel New Media, Comroad and many more

216 Steiner, Klaus „Die Hauptversammlung der Aktiengesellschaft" Munich 1995 at p.84

217 § 131 s.1 s.1 AktG

218 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 131 No. 11

219 § 131 s.2 AktG

220 Steiner, Klaus „Die Hauptversammlung der Aktiengesellschaft" Munich 1995 at p.88

information, or gives it incorrectly, he is threatened to be sentenced to three years' imprisonment or to be fined[221].

To avoid discussions getting out of control, the information right at the general meeting is restricted to the items on the agenda and limited by time, usually five to fifteen minutes. With regard to the timing of the AGM the Landgericht (District Court) Frankfurt ruled[222] that it is not against Company Law to restrict the speaking time and to limit the duration of the AGM in the articles of association.
The requirement by law that the information must be necessary for proper evaluation of an item on the agenda has a more practical meaning in the general meeting than the matters of the company mentioned above. However, it is very difficult to distinguish between information necessary for proper evaluation and irrelevant facts - each case has to be scrutinised on its own merits. Although, it is almost uncontested that this requirement has to be interpreted strictly[223], the corporation is well-advised to be generous in divulging information, especially when its aim is to counter any threatening actions from investors.

Corporate-policy facts necessary for proper evaluation include: numbers, quotes, results, comparisons with competitors or last year's results, achievements (e.g. environmental personnel), future planning, concepts and targets and more. The information does not need to be confined to the business of the year. Often facts of the current business year or of future years may be elements of the general meeting.

Butzke, Hüffer and Decher do not dispute that the additional necessary requirement is that the company's information has to be geared towards an objective shareholder, who is familiar with the conditions of the company due to publicly known facts[224]. However, the vagueness of the legal concept that § 131 s.2 AktG describes leads to a case-related differentiation. In general, it is accepted that information is not given at the general meeting when it is easily accessible elsewhere. To give a better insight into this issue, the figure below provides an overview where the judicature sees information right and where not.

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221 § 400 s.1 no1 AktG

222 Langericht Frankfurt AZ: 3-05 O 93/06 (28.11.2006)

223 Hopt, Klaus J./Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition, 16th delivery §§ 131, 132 Berlin 2001 at No. 133 (Decher)

224 Hopt, Klaus J./Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition, 16th delivery §§ 131, 132 Berlin 2001 at No. 135 (Decher), Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 131 No. 12, Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.246

Figure 16: Information Right - Cases

Part of the Information Right in § 131 s.1 AktG	**Not Part of the Information Right in § 131 s.1 AktG**
Composition of compensation of board members *(e.g. OLG Düsseldorf NJW RR 1997 p.1399, 1400; OLG Düsseldorf NJW 1988 p.1033 and more)*	Composition of compensation of administration members *(e.g. LG Berlin AG 1991 p. 34, 36)*
Qualifications and extent of jobs on the side of board members *(e.g. BayObLG, WM 1996, p.121, 122; restricting OLG Düsseldorf AG 1987 p.21)*	
Inquiries about holdings of more than 5 % (earlier decisions 10%) of the votes or the capital, or with a market value of more than 50 Mio. €uro (controversial position in the literature[225]) *(e.g. BayObLG WM 1996 p.2149; LG Frankfurt WM 1994 p.1930, 1931)*	Inquiries about holdings as far as they are already stated in the annual balance → § 285 No.11, hs.2 HGB *(e.g. KG WM 1994 p.1479, 1485)*
Significant information of positions in the balance sheets or profit and loss *(e.g. BayObLG AG 1996 p. 322, 323; OLG Frankfurt AG 1991, p.206)*	Explanations to the annual balance, which could be deduced from the annual balance *(e.g. OLG Düsseldorf WM 1991 p.2153, 2154; BGHZ 93 p.329, 330)*
Group allocation and transfer prices *(e.g. OLG Karlsruhe AG 1990 p.82)*	Authorship of an analysis *(e.g. OLG Düsseldorf WM 1991 p.2148, 2153)*
Assets of a public limited company, for which the GM has to decide a take-over *(e.g. LG München I AG 1993, p.435, 436)*	Details of internal calculation *(e.g. LG Dortmund AG 1987 p.189)*
Total revenue of donations – not single donations *(e.g. OLG Frankfurt AG 1994 p.39, 40)*	Previous occurrences, which have no effects on the business year *(e.g. OLG Zweibrücken AG 1990 p.496)*
	Reasoning of the pre-emptive right in the case of a capital increase (BGHZ (10.10.2005) - II ZR 148/03)
	Inquiries about properties *(e.g. LG Berlin WM 1994 p.31; LG Frankfurt WM 1994 p.1930)*

It is necessary to restrict the right of the shareholder in the case of an abuse. Personal requitals, insults and ideological speeches are inappropriate when it comes to factual

225 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.250

debates of the general meeting. Therefore the chairman will not face any consequences when he imposes silence on the speaker.
It is also important to point out that prior announcement for the request of information in the general meeting is not necessary.

6.1.4. Right to Refuse Information

The right of the company to refuse information is conclusively listed in § 131 s.3 AktG. The reason for this refusal right is that the legislator has assessed the information right of the shareholder less important than the corporation's right to protect sensitive business material[226]. The company also has the right to refuse to provide the demanded information to a shareholder if the investor could have received the required information from the company's web page.
The introduction of the UMAG in 2005 will give the chairman of the general meeting a powerful tool to restrict the stakeholder's right to address and ask questions of management. According to § 131 s.3 No.7 AktG he will be able to refuse the requested information when the shareholder misused his right. This power can only be executed on the condition that the shareholder assembly has been notified of this rule.

6.1.5. Information Right Outside the General Meeting

§ 131 s.4 AktG extends the information right to the effect that information which was granted to an investor outside the general meeting, has to be given to every other shareholder in the general meeting without any restrictions. Nevertheless, the practical importance of this norm is negligible. Regarding this information right so far no legal proceeding has been successful.

6.1.6. Good Practice Provisions and other Possibilities for Improved Shareholder Information

6.1.6.1. Investor Relations

Closely related to the information right is the concept of investor relations. As its characterisations are numerous, at least the definition of the American National Investor Relations Institute (NIRI) should be quoted here. It defines investor relations as

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226 This includes: data which may place the company at a disadvantage in the marketplace (Standard is the assessment of a responsible businessman); figures relating tax; hidden reserves (holdings, property, intangible assets) – hidden reserves are listed in the balance sheet since the introduction of new international audit standards (IAS or US-GAAP); methods of accounting and valuation; cases where management makes itself liable to prosecution (e.g. data protection); methods of accounting, valuation and clearing with respect to banks and financial institutions (§ 340 ff. HGB); facts relating to insider information § 38 s.1 No. 2 in conjunction with § 14 s.1 No.2 WpHG

> "a strategic management responsibility that integrates finance, communication, marketing and securities law compliance to enable the most effective two-way communication between a company, the financial community, and other constituencies, which ultimately contributes to a company's securities achieving fair valuation"[227].

Taking this into account, investor relations could be seen as a completion of the legally required distribution of information, although their nature as a marketing tool to attract investors is by no means a legal obligation. The methods of conveying material for investor relations are diverse, including brochures, handbooks for investors, press and analyst conferences, one-to-one conversations[228] but also tours of the workplace. Additionally, they use any compulsory publications to transport their information, like annual balances, semi-annual and quarterly interim reports, issue brochures and ad-hoc announcements[229].

Due to the NaStraG, corporations now have a tool to improve their investor relations. The possibility to communicate with the investor, not only on an informative basis but also on a service level, offers corporations a number of advantages. However, incorrect implementation could cause considerable troubles.

Since the NaStraG replaced the words "to send" with "to provide" in § 125 II 1.HS AktG, the legislator made clear that he now also accepts electronic transmission, without standardising the mode of the technology utilised for this purpose. Hence, corporations were able to improve their investor relations service via the Internet.

On account of the fact that the registered shareholder is known by the corporation, the latter is obliged by § 125 II No.3 AktG to get in touch with its investor. This has the undoubted advantage that shareholders are addressed faster, better and more informatively, and the detour via the custodian bank as an intermediary to investor and firm, has become dispensable. This has also led to improved back-office work. The administration of shares could be enhanced in every respect, e.g. dividends could be distributed in a more effective way. Particularly new and small stock corporations, which chose registered shares, profit from these enhanced communication possibilities.

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227 American National Investor Relations Institute (NIRI) - Definition of Investor Relations to download at http://www.niri.org/about/mission.cfm; The differences in the definitions of investor relations are as big as their number. However, as it is not a legal concept, the definition should be left to the practicians. Other examples: Patrick Kiss "Investor Relations im Internet" Wolfratshausen 2001 at p.16-18, Von Rosen, Rüdiger/Gebauer, Stefan „Namensaktie und Investor Relations" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.127-140 at p.129f

228 Von Rosen, Rüdiger/Gebauer, Stefan „Namensaktie und Investor Relations" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.127-140 at p.132

229 Von Rosen, Rüdiger/Gebauer, Stefan „Namensaktie und Investor Relations" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.127-140 at p.131

The flood of new emissions in the late 1990's and early 2000's led to constant ignorance by the economic press and analysts. With the new possibilities the option is given to offset this disadvantage[230].

Intelligent communication with the investor can lead to a healthier attitude of the investor towards the corporation. As mentioned the contact could be used as a basis for customer relations, but more important is the greater loyalty with which the shareholder may handle the shares in his custody. Especially the private investor tends to acknowledge good investor relations with a long investment term[231] and a readiness to extend his custody[232].

However, use of the Internet as a cheap and effective way to contact the investor has the associated danger of abuse of the medium[233]. Publishing price sensitive information is prohibited through § 14 s.1 No.2 WpHG (Prohibition of passing on insider knowledge) and § 15 s.3 s.2 WpHG (Informing in a way other than publishing course-influencing facts). But it was not until the Fourth Finanzmarktfördungsgesetz (Act to Promote the Financial Market) that investor protection was taken very seriously[234].

6.1.6.2. Recognising the Possibilities of Electronic Distribution

6.1.6.2.1. The Electronic Bundesanzeiger (Federal Gazette)

A necessary step was made by the Transparenz- und Publizitätsgesetz (TransPuG) when it introduced the electronic Bundesanzeiger in § 25 s.1 AktG. With this new tool for the shareholder it is not only possible to access recent information from anywhere in the most reasonable way, but also that subscribers could choose to get tailored information. Institutional investors in particular appreciate this new publication form. As they have to rely on the most topical general meeting information, the electronic access is a considerable improvement, especially in view of the fact that material provided by issuers or custodians often is inaccurate. Proxy voting services can also profit from this new tool as they now can improve delivery speed and access to their shareholder services.

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230 Von Rosen, Rüdiger/Gebauer, Stefan „Namensaktie und Investor Relations" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.127-140 at p.135

231 Heidorn, Thomas/Schmidt, Peter/Seiler, Stefan „Neue Möglichkeiten durch die Namensaktie" Work Report No. 23 Hochschule für Bankwirtschaft and Kreditwesen 5/2001 at p.32

232 Von Rosen, Rüdiger/Gebauer, Stefan „Namensaktie und Investor Relations" in Von Rosen, Rüdiger/Seifert, Werner G. "Die Namensaktie" Schriften zum Kapitalmarkt Band 3, Eschborn 2000 also to download at http://www.dai.de/internet/dai/dai-2-0.nsf/dai_publikationen.htm p.127-140 at p.135

233 Handelsblatt 25.09.01 „Aktionär gewinnt gegen Neue-Markt-Firma" Infomatec-Fall/Falsche Ad-hoc-Mitteilung

234 To gain a good overview about the problem of rate influencing facts, with spezial regard on § 14 I Nr.2 and § 15 Abs.3 Satz 2 WpHG → Ekkenga, Jens „Kapitalmarktrechtliche Aspekte der „Investor Relations"" in Noack, Ulrich/Spindler, Gerald"Unternehmensrecht und Internet" Munich 2001 at p. 101- 121

6.1.6.2.2. Notice to the General Meeting

The NaStraG has enabled corporations to give notice of shareholders' meetings in electronic form. Sending notice of the general meeting in such a format saves the company a considerable amount of postage fees[235] and administrative work. However, to use the Internet as a distribution channel it is necessary to have the e-mail address of each shareholder. Hence, spreading information only electronically is almost impossible for the company issuing bearer shares (custodian banks have not yet shown their intention to adopt the Internet as an informing tool). For companies with registered shares, however, this point is far more interesting as the system is currently in use and being refined. Although the switch to distribute shareholder information via the Internet will incur intensive set-up costs and will be a longstanding process, the result will significantly reduce distribution, administration and time costs. Therefore it is quite incomprehensible that the planning of the vast majority of the stock corporations is not heading in this direction.

The corporation is obliged to give notice of the shareholders' meeting to all shareholders, at least to maintain their activism and meet their assignment of corporate governance. According to § 125 IV AktG, it is sufficient to make decisions of the shareholders' meeting accessible to the shareholder on the Internet. However, it needs to be remarked critically that the Internet is not yet a means of mass media like television[236] and that, therefore, some sections of the population might have problems in obtaining the desired information. So the offer of the corporation to send the decisions (hard or soft copy) upon investors' requests is sufficient legally, and economically reasonable for businesses.

For the providers of proxy voting services, which have electronic contact information for their clients, the decisions of the meeting could easily be attached to the voting reports, which are already sent electronically, providing that the issuers are willing. Having said that, it should be remarked that although the law states that the electronic publication (§ 125 s.4 AktG) is equivalent to hard copy reports, still a number of corporations and custodians prefer the latter.

6.1.6.2.3. Countermotions

Since the introduction of the TransPuG in 2002 it is legally possible to publish countermotions of shareholders on the company's webpage (§ 126 s.1 s.1 AktG). At first glance active shareholders will view their rights as having been reduced, but this new

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235 The Deutsche Börse Systems estimated that 20.000 shareholders with 250.000 transfers will cost a corporation 2,19 Euro per shareholder per year. - Börsen-Zeitung 27.01.2000 "Börse präzisiert Aktienbuch-Kosten"

236 Spindler, Gerald „Internet und Corporate Governance - ein neuer virtueller (T)Raum?" Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 2000 at p.429

practise will bring a number of improvements. Notably deadlines for countermotions could be cut to two weeks prior to the general meeting. Although it will become more difficult to make other shareholders aware of the countermotion, as they would rarely check the company's webpage for opposing views on items of the agenda, the quality of reply will be enhanced. In any case the opposing shareholder will formulate his countermotion at the general meeting, where he has the opportunity to make other investors aware of his issue for a second time. Additionally, communication among the shareholders would be improved.

6.1.6.2.4. Shareholder Forum

With respect to enhanced shareholder pluralism, the introduction of a shareholder forum within the electronic Bundesanzeiger (according to § 127a AktG) has to be welcomed. Accordingly, it is now possible for shareholders to communicate and coordinate themselves with the aim of executing their shareholder rights. For instance in those cases where the legislator requires certain thresholds: such as the calling for a general meeting (§ 122 AktG), the special accounting (§ 142 s. AktG) and the request for compensation (§ 147 s.2 s.2, § 147a s.1 AktG)[237].

This provision is the consequence of an increasing free float and an ongoing internationalisation of the shareholder structure, as well as the recognition that it is not possible for holders of registered shares to make use of the register, and the anonymity of the investors in bearer stocks[238].

6.1.6.2.5. Further Application of the Internet

Another field of application of the Internet is that of "Shareholder Boards". With their help shareholders are able to communicate among each other as the general meeting approaches. Noack suggests a commitment of the corporations to install such a board on its own website to improve the possibility to achieve capital presence and aid coordination among shareholders[239].

If the articles of association provide the possibility to transmit the AGM in picture and sound, the AGM could also be broadcasted via the World Wide Web, making the full length AGM accessible to connected shareholders worldwide. This facilitates various levels of service, for example if the company decides not only to broadcast the meeting

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237 Seibert, Ulrich/Schütz, Carsten „Der Referentenentwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts - UMAG" in Zeitschrift für Wirtschaftsrecht (ZIP) 2004 p. 252-258 at p. 255; Bundesjustizministerium "Entwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" 2004 to download at http://www.bmj.bund.de/media/archive/701.pdf at § 127a AktG

238 Seibert, Ulrich/Schütz, Carsten „Der Referentenentwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts - UMAG" in Zeitschrift für Wirtschaftsrecht (ZIP) 2004 p. 252-258 at p. 255; Bundesjustizministerium "Entwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" 2004 to download at http://www.bmj.bund.de/media/archive/701.pdf at § 127a AktG

239 Noack, Ulrich „Moderne Kommunikationsformen vor den Toren des Unternehmensrechts" Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 3/1998, S. 592-616 and to download at http://www.jura.uni-duesseldorf.de/dozenten/noack/texte/noack/kommunik.htm at IV 1

but also to allow online voting or the request to address the forum. Although some stock corporations already have offered a live-transmission of their AGM via the Internet and proxy voting via the web, doubt arises regarding the on-line request to speak or pose questions. This is due to understandable reluctance of corporations to widen the right to speak at AGMs often exceeding a thousand investors, but also because of the increased danger of legal conflicts initiated by shareholders who overestimate their role.

With respect to transmission in picture and sound, it is important to mention the fact that the legislator does not see problems regarding the right of personality. As it is unreasonable to demand that an on-line viewer sits in front of a black screen because the current speaker does not want his speech transmitted, it is reasonable for the orator to appoint a representative, who will speak on his behalf[240].

If the articles of association provide this option, then it is possible for members of the supervisory board to also participate via video and sound (§ 118 s.2 AktG). Members of the management board have the duty to inform investors at the meeting while reducing the presence requirements of shareholder representatives, especially from abroad, is not regarded as counterproductive[241].

It should be documented that further applications of the Internet with regard to publication requirements are already manifested in the law or being drafted. For example the requirement to publish the investors' subscription rights[242] also has to be made accessible electronically. Also there is demand to publish the remuneration of the management on the company's web pages according to the German Corporate Governance Code[243].

It should not be neglected that intermediates also make extensive use of the electronic distribution channels. For them this is a perfect sales argument as clients save postage fees and are enabled to automate some of the processes in conjunction with the general meetings.

6.1.6.2.6. Conclusion

Certainly, the Internet is more than suitable for distributing any information, including publicity, in a reasonable way. This makes it quite attractive to stock corporations, especially for the investor relations departments. With regard to a number of provisions, especially the Bundesanzeiger, which have the obligation of disclosure, it

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240 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Reform des Aktien- und Bilanzrechts, zu Transparenz und Publizität (Transparenz- und Publizitätsgesetz)" 2002 to download at http://www.bmj.bund.de/media/archive/301.pdf at reasoning of § 118 s.3 AktG

241 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Reform des Aktien- und Bilanzrechts, zu Transparenz und Publizität (Transparenz- und Publizitätsgesetz)" 2002 to download at http://www.bmj.bund.de/media/archive/301.pdf at reasoning of § 118 s.2 AktG

242 § 186 s.2 s.2 AktG

243 Especially foreign investors believe that the information policy with regard to management renumeration in Germany is considerably poor.

has to be acknowledged that the Internet is so far only able to be an additional tool to distribute information.

However, if the issuers exhausted the good practice provisions and other possibilities for improved shareholder information, they could not only adjust their investor relations more effectively but could also put the shareholders in a position in which they could assess the corporate performance more easily, especially with regard to corporate governance.

Finally, the Transparency Directive[244] (2004) of the EU should be mentioned. Its declared aim is to improve investor protection and boost market efficiency. To that end, it also seeks to ensure greater openness to the world of international finance in terms of use of languages and the more widespread use of modern technologies to disseminate information[245]. However, its impact on the information provided by the issuers will only be minor. As the European Economic and Social Committee explains:

> "It must be borne in mind that the proposed directive seeks not maximum, but minimum harmonisation."[246]

Having explained the information right I will now introduce the next form of engagement according to the introduced hierarchy. Shareholder negotiations are an instrument, which is, in contrast to the other forms of engagement, not regulated by Company Law.

6.2. Shareholder Negotiations

Shareholder negotiations (including informal discussions as a "softer" form of negotiations) are an alternative to the tools provided to the shareholders by the different legal systems. Institutional or other influential investors, rather than small private shareholders, have the option to inform the management of their interests in another fashion than through proxy voting or buyouts. As has been shown above, shareholder negotiations, for instance, often provide a more positive impact on corporate performance than voting on an agenda item. Pound stated that the most significant aspect of the new political process (shareholder power) is the rise of informal political mechanisms to supplant, and even replace, the extreme measure of the formal

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244 European Parliament and the Council "Directive 2004/109/EC of the European Parliament and of the Council - of 15 December 2004 - on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC" Official Journal of the European Union, Issue L390 (31.12.2004) p.38-57

245 Opinion of the European Economic and Social Committee on the "Proposal for a Directive of the European Parliament and of the Council on the harmonisation of transparency requirements with regard to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC" Official Journal of the European Union, Issue C80 (30.04.2004) at p.128

246 Opinion of the European Economic and Social Committee on the "Proposal for a Directive of the European Parliament and of the Council on the harmonisation of transparency requirements with regard to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC" Official Journal of the European Union, Issue C80 (30.04.2004) at p.129

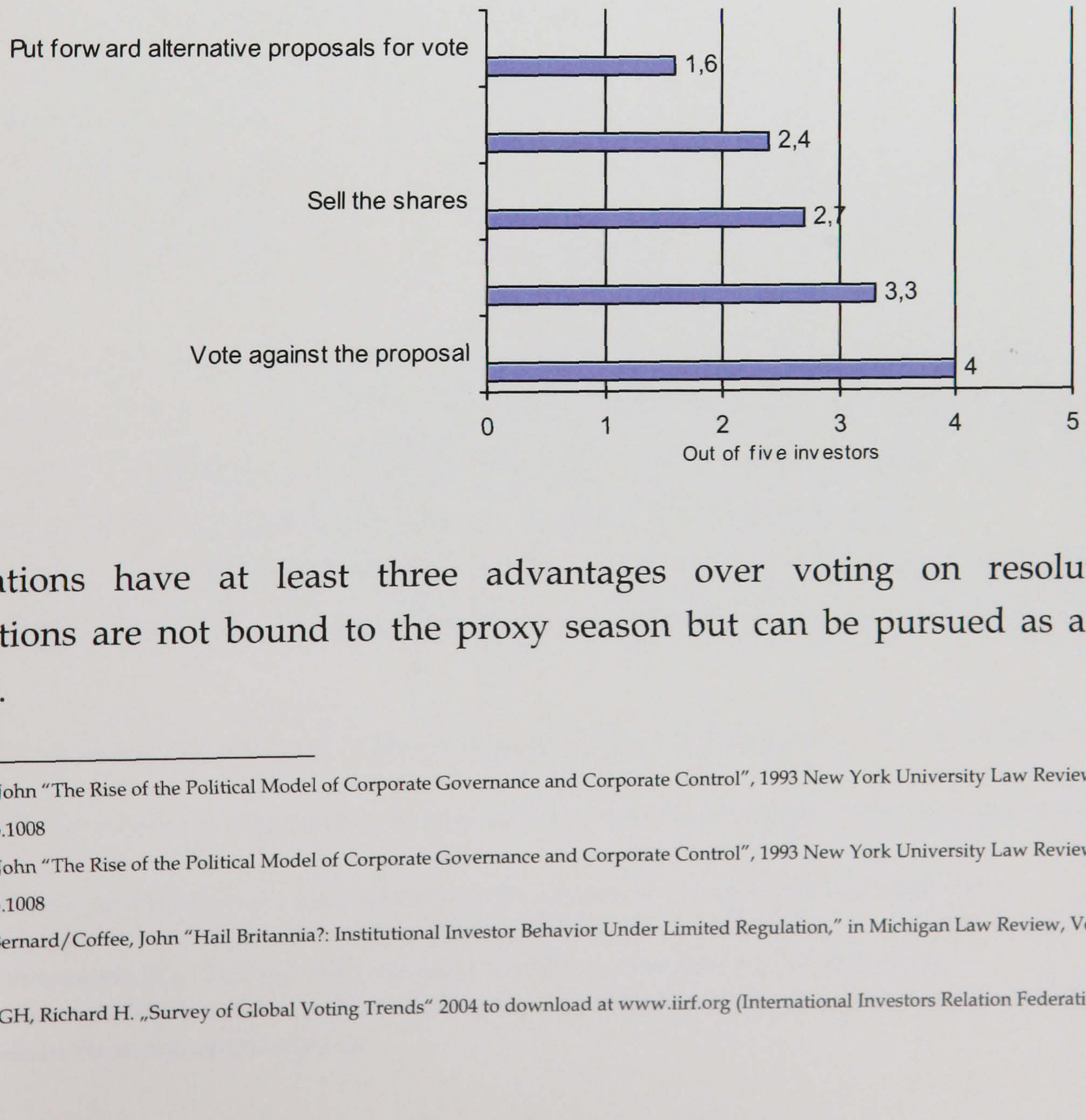
voting challenge[247]. Although this statement is contentious it shows that investors are well-advised to take into account additional measures than those provided by Company Law. The examples provided by Pound of successful shareholder campaigns at IBM, American Express, Eastman Kodak, Kmart[248] and Daimler Chrysler support this assessment.

Shareholder negotiations are a form of engagement not based on legal provisions. This advantage to "bargain in the shadow of the law"[249] allows the investor to see them as a preliminary stage to general meeting resolutions and litigation. The position "outside the law" leaves the parties sufficient room to find an agreement and to move forward in a common sense. Legal limits might not only endanger the success of the negotiations and other measures, which are not regulated in the Company Law, but will also draw a wall between the owners and the issuers and will certainly foster overregulation.

6.2.1. Shareholder Negotiations as a Supplementing Tool

As it can be seen in figure 17, one popular tool used by institutional investors after voting is shareholder negotiation or informal discussion.

Figure 17: Action Taken by Investors[250]



Negotiations have at least three advantages over voting on resolutions. First, negotiations are not bound to the proxy season but can be pursued as a year-round activity.

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247 POUND, John "The Rise of the Political Model of Corporate Governance and Corporate Control", 1993 New York University Law Review Volume 68 No.5 pp. 1003-1071 at p.1008

248 POUND, John "The Rise of the Political Model of Corporate Governance and Corporate Control", 1993 New York University Law Review Volume 68 No.5 pp. 1003-1071 at p.1008

249 BLACK, Bernard/Coffee, John "Hail Britannia?: Institutional Investor Behavior Under Limited Regulation," in Michigan Law Review, Vol. 92, 1994, p.1997-2087

250 GRUBAUGH, Richard H. „Survey of Global Voting Trends" 2004 to download at www.iirf.org (International Investors Relation Federation) Figure 21

Second, it has to be recognised that dialogue and strategic campaigning could be better means of achieving corporate change than resolutions. While the latter could target only a limited number of agenda items at a certain point of time, shareholder negotiations could cover broader issues over a longer period and thus also have strategic advantages. In contrast to the attempt of improving corporate performance by voting on an agenda item, which will most probably fail, it could be claimed that the management could prove to be more flexible in negotiations as in the end they could claim an outcome as their success.

A third advantage of shareholder negotiations is suggested by Black and Coffee[251]. They assume that both sides, investors as well as corporations, can lose from voting contests. This could explain the strong preference for behind-the-scenes settlements. Both sides have reason to threaten steps that are costly to them, hoping that a bluff will work. By "bargaining in the shadows", costs, including reputational damage to individuals and institutions, can be minimised[252].

However, I would also argue that shareholder negotiations have the greatest impact when they are used as a supplement tool. Dubiel[253] points out that normally the company would be informed of a shareholder issue before a voting recommendation is given. This gives the stock corporation the opportunity to react and make necessary changes. Consequently, the shareholder is well advised to begin the engagement by searching for a dialogue with the company before they formulate a proposal to the general meeting. Carleton, Nelson and Weisbach[254] describe this process as follows:

> "When an institution has an issue it is concerned about, it typically will contact a firm privately about the issue first. Depending on the firm's response, the institution will determine whether to file a proxy resolution. The process potentially is repeated for several years until either the firm changes its policy or the institution decides not to pursue matters further."

A good example that supports this hypothesis is the Daimler Chrysler AGM in 2004. Negotiations prior to the AGM showed the management that a vast majority of shareholders intended to oppose the proposed remuneration of the management. Consequently, the boards decided to withdraw this agenda item.

The findings of Gillian and Starks[255] also support this statement. According to their study, negotiations lead to an increase of withdrawals of shareholder proposals. In the

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251 BLACK, Bernard/Coffee, John "Hail Britannia?: Institutional Investor Behavior Under Limited Regulation," in Michigan Law Review, Vol. 92, 1994, p.1997-2087

252 BLACK, Bernard/Coffee, John "Hail Britannia?: Institutional Investor Behavior Under Limited Regulation," in Michigan Law Review, Vol. 92, 1994, p.1997-2087 at p.2054

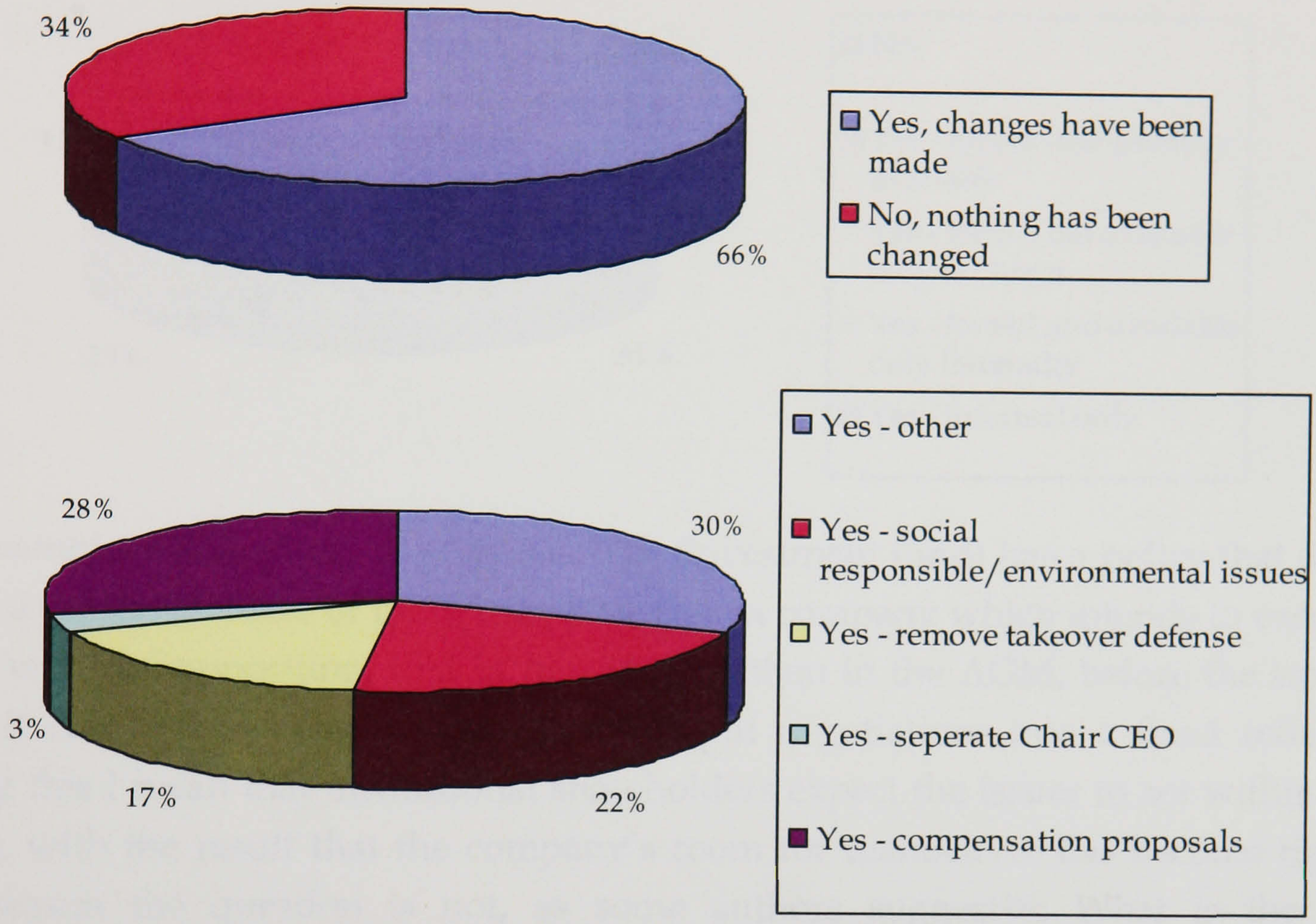
253 DUBIEL Stanley - Vice President of Institutional Shareholder Services - personal interview held on the 13th of January 2005

254 CARLETON, Willard T. / NELSON, James M. / WEISBACH, Michael S. „The Influence of Institutions on Corporate Governance through Private Negotiations: Evidence from TIAA-CREF" in The Journal of Finance, Vol. LIII, No. 4, August 1998 at p. 1335-1362 at p.1335

255 GILLIAN, Stuart L. / STARKS, Laura T. "Corporate Governance Proposals and Shareholder Activism: the Role of Institutional Investors" in Journal of Financial Economics, Vol. 57, 2000 at p.275-305 at p. 296

years 1987-1994 they investigated 2042 proposals of which 244 were withdrawn following shareholder negotiations[256].
To point out the impact of shareholder negotiations, figure 18 provides an idea of its success rate. It shows the response rate of issuers as a result of shareholder pressure.

Figure 18: Changes in Strategy, Policies or Disclosure have been made or not as a Result of Shareholder Pressure[257]



Although this figure does not show the exclusive response rate to shareholder negotiations but to other instruments of shareholder engagement like voting, the number of two thirds is considerable and gives proof to the fact that shareholder engagement could lead to the desired aims[258].

For the successful outcome of shareholder negotiations in Germany the subject of the negotiations plays a decisive part. It is understandable that an agreement on less far-reaching issues like changing a stock option is easier to achieve than radical changes of the statutes or dismissing the CEO. Additionally, the ownership structure also plays an important role. The management of a company where the stocks are widely held is certainly more responsive than the management of a company where 50% of the stocks are concentrated.

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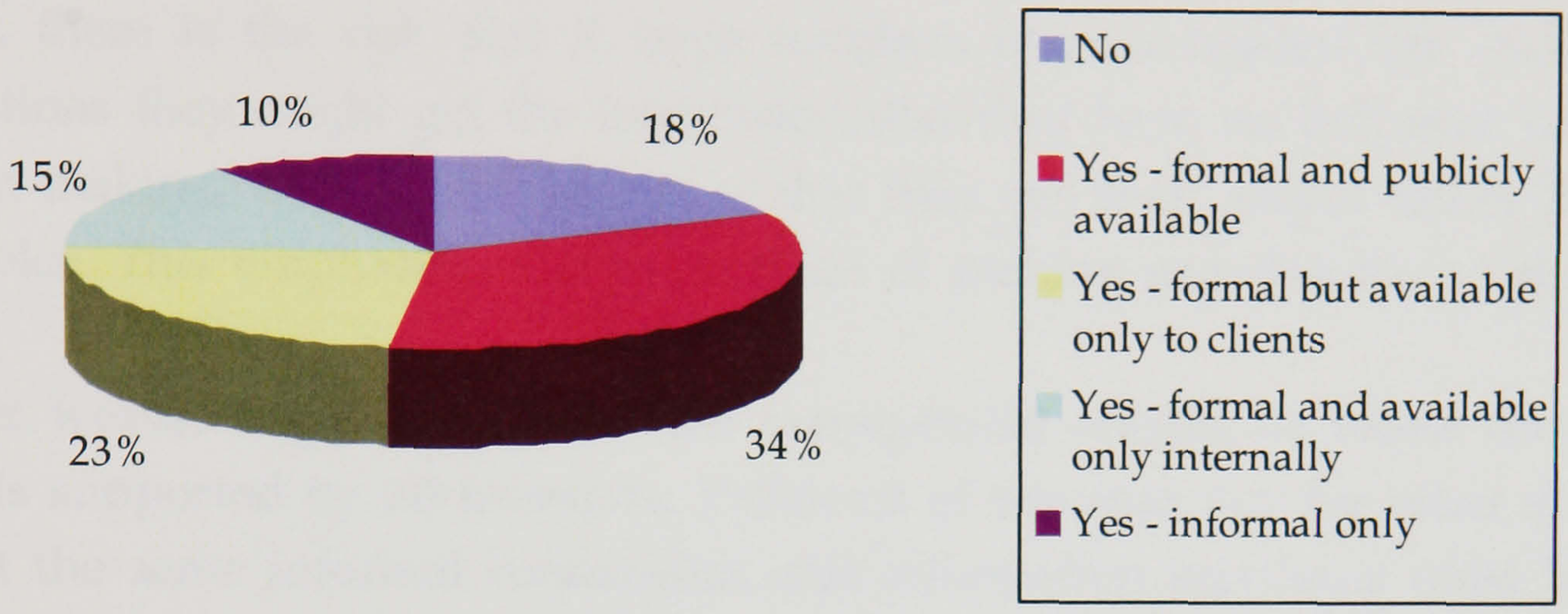
256 GILLIAN, Stuart L. / STARKS, Laura T. "Corporate Governance Proposals and Shareholder Activism: the Role of Institutional Investors" in Journal of Financial Economics, Vol. 57, 2000 at p.275-305 at p. 297

257 GRUBAUGH, Richard H. „Survey of Global Voting Trends" 2004 to download at www.iirf.org (International Investors Relation Federation) Figure 25

258 Same result in CARLETON, Willard T. / NELSON, James M. / WEISBACH, Michael S. „The Influence of Institutions on Corporate Governance through Private Negotiations: Evidence from TIAA-CREF" in The Journal of Finance, Vol. LIII, No. 4, August 1998 at p. 1335-1362 at p.1357

Moreover, it is important to understand that to increasing extent institutional investors formulate their own corporate policies or use those of a third party[259]. In doing so a strict standard is applied not only for voting but also for negotiations. Consequently, institutional investors only have limited room for negotiations. The following figure gives proof of this assessment.

Figure 19: Does the Institutional Investor Have a Voting Policy?[260]



For example, if a Kapitalanlagegesellschaft (investment fund) has a policy that does not allow a capital increase of more than 20%, then a company which intends to exceed this mark will face opposition, first in negotiations then in the AGM, before the stocks are sold. It can be observed that this practice put negotiations into a fixed scheme. By saying this I mean that institutional shareholders expect the issuer to act within the set frame, with the result that the company's room for manoeuvre has become tight. For this reason the question is not, as some authors suggest[261]: What is the subject shareholders target most often? It is rather: Where are issuers most likely to exceed the limits? To be more precise, the investment funds only have limited room to manoeuvre within their corporate policy. In contrast to that the company could create its own guiding principles. Certainly this development restricts entrepreneurial freedom to a certain extent, but it has the advantage that political standards are set for the companies. This could save costs and efforts on both sides.

Finally it needs to be added that Carleton, Nelson and Weisbach discovered that insider-controlled firms are less concerned about their reputation with shareholders and thus are less open for negotiation but are more willing to let the issues go to a proxy vote[262].

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259 e.g. DSW – Deutsche Schutzvereinigung für Wertpapierbesitz, Institutional Shareholder Services

260 GRUBAUGH, Richard H. „Survey of Global Voting Trends" 2004 to download at www.iirf.org (International Investors Relation Federation) Figure 5

261 CARLETON, Willard T. / NELSON, James M. / WEISBACH, Michael S. „The Influence of Institutions on Corporate Governance through Private Negotiations: Evidence from TIAA-CREF" in The Journal of Finance, Vol. LIII, No. 4, August 1998 at p. 1335-1362

262 CARLETON, Willard T. / NELSON, James M. / WEISBACH, Michael S. „The Influence of Institutions on Corporate Governance through Private Negotiations: Evidence from TIAA-CREF" in The Journal of Finance, Vol. LIII, No. 4, August 1998 at p. 1335-1362 at p.1349

6.2.2. Limits of Shareholder Negotiations

When pointing out the limitations of shareholder negotiations it is essential to stress their shortcomings.
First, shareholder negotiations usually do not create a short-term reaction on the stock market as the results will probably be kept confidential. However, at least they have the potential to create some shareholder value on a long-term basis.

Second, there is the risk that if large numbers of shareholders are excluded from negotiations they might get the impression that they have no influence on corporate decision making, with the consequence that they sell their shares rather than raising their voice. This emphasises the importance of making negotiations a "shareholders' issue"
In other words, negotiations with the management should be based on an interest which is supported by all investors. Problems of transparency for other shareholders without the same informal concessions and information privileges must be avoided. Although the option to benefit from the negotiations without getting involved (free-riding) will leave the excluded shareholders inactive, it will be favourable to inform them of discussions. Especially, private shareholders might have difficulties in assessing the company's present situation accurately.

In addition to that, unless other significant institutions participate, there is the danger that efforts by a single shareholder fail due to insufficient pressure and influence. Strenger points out that, institutional investors in Germany have not been coordinating their engagement sufficiently so far. In contrast to other countries[263] German investors rarely form alliances. The consequence is that their voices often do not get the desired hearing[264]. The reason for this lack of coordination needs to be seen historically. Usually, it were the custodian banks who determined corporate policy. Not until the last couple of years (probably starting with the introduction of the NaStraG in 2001) the legislator as well as clients demanded that institutional investors should pursue more responsible investment, which included the safeguarding of fiduciary duties. Only slowly institutional investors recognise their responsibility and start to emancipate from (in-house) custodian banks.

Just like that the share of foreign investors is mostly insufficient to raise corporate issues to the interest of other investors, providing that there is actually an interest. Additionally, the opinion is still widely spread that criticising the management is a form of activism which produces negative publicity.

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263 Examples include the forming of primarily Anglo-American alliances to address issues at ABN Amro (2007), Deutsche Börse (2005) or CeWeColor (2007)

264 STRENGER, Christian - Member of the Cromme Commission and chairman of the supervisory board of DWS (Germany's biggest fund company) - personal Interview held 10th of Jan. 2005

The result is that primarily institutional investors neglect the option of communicating and forming alliances with fellow shareholders.
Moreover, it has to be recognised that the position of small private shareholders is too weak anyway. Although they have the possibility to coordinate themselves through web-based platforms, their influence will still be too negligible for the management to take up raised issues.
Especially with respect to institutional investors this reluctance towards coordinated engagement in Germany needs to be overcome. Firstly, a common voice of the shareholders will show the management that there is indeed an issue that cannot simply be ignored. Secondly, it will strengthen the position of engaged investors towards those who prefer selling the shares (Exit Versus Voice). Finally, a coordinated action could make the administration easier, avoid the free rider problem and consequently, save costs.

Besides that, it has to be recognised that institutional investors do not have a sufficient infrastructure to pursue responsible engagement. For instance, they do not have an electronic voting platform; cover national meetings only; have no defined corporate policy; still rely on their in-house custodian or do not have the experience to pursue sound shareholder engagement.

Moreover, in general their influence in negotiations or general meetings is not proportional to their share. Often success is achieved by chance. Only when the broad number of shareholders or even the public raises interest in certain issues more coordinated activity is recognisable. A good example in this respect is the Daimler Chrysler AGM in 2004. Here a number of investment funds publicly announced that they did not intend to approve the acts of the management. At the end the DaimlerChrysler management received an approval of "only" 88%.

In this respect it has also to be recognised that sometimes a strong interest, carried by the public opinion or the shareholders towards the management is necessary to pave the way for negotiations. While it is relatively easy to play down issues raised by small shareholders, it is not advisable to ignore majorities.

Another universally applicable issue is raised by Brennan[265]. He states that in general experience also exposes the limitations of shareholder negotiations:

> "Shareholder disputes reveal the relative power of capitalist firms to manage the assets of shareholders according to their own capitalist wishes. ..... When companies face challenges from

265 BRENNAN, David M. ""Fiduciary Capitalism," the "Political Model of Corporate Governance," and the Prospect of Stakeholder Capitalism in the U.S.", 2003 to download at http://www.newschool.edu/cepa/papers/workshop/040910_Brennan.pdf also in Review of Radical Political Economics, Vol. 37, n° 1 - winter 2005 at p.39-62

> shareholder resolutions, they often produce their own persuasive rhetoric in defence of current business practices to sway public and shareholder opinion. ..... Their responses demonstrate clearly that corporations are willing and able to argue persuasively against seemingly "popular" shareholder issues. In part because of savvy corporate public relations, shareholder resolutions face the difficult task of getting enough votes to change corporate policy. This issue has lasting significance, because shareholder resolutions represent a significant challenge to corporate behaviour; as businesses defeat these resolutions, corporations severely weaken shareholders' power to negotiate issues of corporate governance."

Finally and most importantly, it needs to be pointed out that the outcome of shareholder negotiations will typically lack a "legal base". It will not, in other words, result in an agreement that is binding upon the company. As a result some uncertainty will always remain. However, when misgivings following negotiations come true, the general meeting provides a perfect platform to remind the other party of the outcome of the negotiations.

6.2.3. Using the Publicity to Support Shareholder Negotiations

Shareholder negotiations (as well as other forms of engagement) are sometimes supported by public campaigns. A crucial factor with those campaigns is that they are mostly driven by the media and less by investors. The latter might initiate the campaign but cannot control its content or direction. Therefore campaigns are not a form of controlled shareholder engagement, although the investor might seek the support of public campaigns.

A successful example of a public campaign is provided by the case of the U.K. based Hedge Fund TCI. In connection with the Deutsche Börse bid for the London Stock Exchange in 2005, the fund (which owned about 8% of the Deutsche Börse) announced that it refused to support the attempts by the German company. Other primarily Anglo-American investors followed TCI's example with the result that the CEO of the Deutsche Börse had to withdraw the offer. Prior to the AGM 2005 the CEO and the chairman of the supervisory board of the Deutsche Börse resigned.

However, campaigns often are not in the interest of shareholders as their result is mostly negative. The stock price suffers and the image of the company could be harmed lastingly. A good example in this respect is the Mannesmann case in 2004, where a public campaign on excessive management compensation was pursued. Not only were the involved managers heavily criticised, but also the stock price of the affected companies (e.g. Deutsche Bank) was put under pressure. This example indicates that public campaigns are often populist levers rather than an instrument to be used to implement a desired corporate change. Consequently, Strenger points out that a public campaign could only be one of the last options for institutional investors as negotiations

regularly promise better results[266]. If an investor decides that his engagement needs the support of a public campaign he needs to be aware of the fact that he will not be able to control the campaign.

6.2.4. Conclusion

For the investor it is well worth considering alternative forms of engagement to those provided by Company Law. As it has been shown, shareholder negotiations carry the shareholders' interest to the management's attention and further. This is based on the assumption that this form of engagement might be more cost effective than other forms provided by Company Law and that it could be more successful when used supplementary to the tools provided by Company Law.
Unfortunately, there is no documentation showing to what extent shareholder negotiations are successful.

Finally I would like to complement the following universally applicable observation of Brennan[267].

> "When an investor fails with a proposal to negotiate a certain issue or similar measure he still could propose a shareholder resolution in the AGM or file a suit."

When an investor prefers to submit a counter proposal or to go to court first and is unsuccessful, his chances of negotiating a compromise with the management later are considerably limited. This statement is supported by the assumptions of Galanter[268]. According to him, "settlements" entail "bargaining in the shadow of the law," so the influence of legal doctrine is present but is thoroughly mixed with considerations of expense; delay; publicity and confidentiality; the state of the evidence; the availability and attractiveness of witnesses; and a host of other contingencies that lie beyond the substantive rules of law. It is "the law" in its broad sense of process that casts the shadow, not merely its doctrinal core."[269]

The described shareholder negotiations are a relatively "informal" way of engagement. Following the hierarchy of shareholder engagement, the Stock Corporation Act provides further "formal" forms of activity the investor could pursue. Having already

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266 STRENGER, Christian - Member of the Cromme Commission and chairman of the supervisory board of DWS (Germany's biggest fund company) - personal Interview held 10th of Jan. 2005

267 BRENNAN, David M. ""Fiduciary Capitalism," the "Political Model of Corporate Governance," and the Prospect of Stakeholder Capitalism in the U.S.", 2003 to download at http://www.newschool.edu/cepa/papers/workshop/040910_Brennan.pdf

268 GALANTER, Marc „The Vanishing Trial: An Examination of Trials and Related Matters in Federal and State Courts" in Journal of Empirical Legal Studies, Volume 1, Issue 3, November 2004, p.459–570 at p.525

269 GALANTER, Marc „The Vanishing Trial: An Examination of Trials and Related Matters in Federal and State Courts" in Journal of Empirical Legal Studies, Volume 1, Issue 3, November 2004, p.459–570 at p.525

introduced the information right, the following chapter will describe the right to speak at the general meeting.

6.3. Speaking at the General Meeting

Another shareholder engagement right Company Law recognises is speaking at the general meeting. Its nature is closely related to the information right, as § 131 AktG provides the right to speak in order to obtain information. As this shareholder right does not bear any consequences it plays a less important role legally than politically. This derives from the fact that speaking at the general meeting can be an effective tool to express discontent or satisfaction with the management's performance. It needs to be acknowledged that constructive criticism is formulated in few cases only. Mostly only asset managers or representatives from shareholder associations stick to the agenda and specify their concerns. In numerous other cases, however, the right to speak at a general meeting is frequently abused, which makes an efficient carrying through of the general meeting almost impossible. The tendency to use the lectern in the general meeting as a platform to pursue ideological aims, to perform showmanship[270], to advertise products or even for cultural contributions distorts the purpose of the general meeting. An excellent example is the Daimler Chrysler AGM in 1993, where Prof. Wenger was forced to leave as he worded his criticism of the management too rudely[271].

Therefore it was only a consistent development that with the introduction of the UMAG the authority of the chairman was increased to the extent that he now has the possibility to limit the time of the shareholder to speak or to ask his questions. This measure to make the shareholder assembly more efficient has been expected for quite some time[272]. According to the Stock Corporation Act, the right to speak should give the shareholder the opportunity to make an inquiry and to specify his information request. Here it must be accepted that the "inquiry" may turn out to be a corporate political speech. Although this serves the dialogue between the shareholders and management, it is necessary that during the shareholder meeting certain rules are applied in order to maintain a qualitatively high standard while removing cumbering factors.

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270 Brost, Marc/Heuser, Uwe Jean „Das sind absurde Zustände" Interview with Hilmar Kopper in „Die Zeit" 18th Issue 2001to download at http://www.zeit.de/2001/18/Wirtschaft/200118_beistueck_corpor.html; Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.214

271 Manager Magazin „Schreck aller Vorstände" 23.11.2004 to download at http://www.manager-magazin.de/unternehmen/artikel/0,2828,329294,00.html

272 E.g. Brost, Marc/Heuser, Uwe Jean „Das sind absurde Zustände" Interview with Hilmar Kopper in „Die Zeit" 18th Issue 2001to download at http://www.zeit.de/2001/18/Wirtschaft/200118_beistueck_corpor.html

6.4. Shareholder Proposal or Calling a General Meeting

§ 122 AktG provides that shareholders holding 5% or 500,000 Euro of the capital stock are entitled to request the announcement of agenda items to be decided in the general meeting. Additionally, shareholders who hold together more than 5% of the capital stock have the right to call a general meeting. The same rights are also granted to single shareholders who meet these requirements.

Therefore to a certain extent, § 122 AktG serves the separation of powers between the shareholders, the management board and the supervisory board[273]. This possibility for the shareholders supports the critical dealing with the company and avoids a diktat of the agenda by the management.

The latter is obliged to execute the request of the shareholders and has no latitude. Only when the formal requirements are not met; the general meeting is not responsible; the resolution is illegal; not in accordance to the statutes or the request is abused, an action is unnecessary[274].

With respect to formal requirements it needs to be pointed out that the argument for requesting the announcement of a shareholder proposal does not need to be made substantiate; it is sufficient that the argument is designated.

More complex is the discussion about the abuse of the rights according to § 122 AktG. However, to maintain the protection granted by § 122 AktG, high demands are made to classify a request as being used improperly[275].

For instance, the right to file a shareholder proposal is assumed to be abused when[276]:

-an item should be put on the agenda, although an earlier general meeting already dealt with the issue and circumstances have not changed since.

-the resolution insults or obviously provides false or misleading statements.

-the item is obviously superfluous or does not serve the pursuit of shareholder interests, but intends to harm the company.

-there is an easier way to achieve the desired aim.

-the approval of a third party is required, while it is certain that the approval will not be given

It is also an abuse to call a general meeting if the next general meeting could deal with the agenda item and thus no urgency is given.

However, it needs to be made clear that a resolution is not improper simply because it could never expect a majority of votes.

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273 Halberkamp, Thomas/Gierke, Olaf „Das Recht der Aktionäre auf Einberufung einer Hauptversammlung" in Neue Zeitschrift für Gesellschaftsrecht (NZG) No. 11/2004 p.494-502 at p.495

274 Halberkamp, Thomas/Gierke, Olaf „Das Recht der Aktionäre auf Einberufung einer Hauptversammlung" in Neue Zeitschrift für Gesellschaftsrecht (NZG) No. 11/2004 p.494-502 at p.495

275 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 122 no 6

276 Halberkamp, Thomas/Gierke, Olaf „Das Recht der Aktionäre auf Einberufung einer Hauptversammlung" in Neue Zeitschrift für Gesellschaftsrecht (NZG) No. 11/2004 p.494-502 at p.498

In the case that the board rejects the calling of a general meeting or the announcement of an agenda item, the course of law is provided by § 122 s.3 AktG.

Even where minority shareholders are successful with their request for a new agenda item, the general meeting is not obliged to deal with it and could simply decide to take the item off the agenda[277]. However, the general meeting, respectively the management, is well advised to approach this decision carefully, as shareholders are bound by their duty of loyalty and as the board should avoid taking sides in this matter. It is recommendable that the chairman explains that a decision to take the item off the agenda will be equal to a vote against it. This approach would make the holding of the meeting more economical[278].
It should be made clear that the costs for a successful shareholder request according to § 122 s.1 and s.2 AktG have to be covered by the company.

The right to call a general meeting serves the protection of minority shareholders and facilitates the participation right, the right to file a suit, and the execution of shareholder rights with regard to the general meeting[279]. This means the request to call a general meeting is virtually less important than the request to announce a shareholder proposal. Although investors make less use of this right today than in the late 1990s, Butzke explains that § 122 s.2 AktG has often been abused to supplement the agendas of DAX-companies by often identical, socio-political items, which obviously did not serve the prosperity of the corporation[280]. This abuse was largely stopped as a result of the critical scrutiny of the formal and material right mentioned above.

6.5. Voting Right

The most powerful tool of the investor beside the right to sue is the voting right, allowing the shareholder to verbalise his opinions towards management and the meeting issues. Here the connection between shareholder engagement and corporate governance becomes most obvious, as corporate policy is directly influenced.
The possibility to co-determine corporate policy is given by § 12 s.1 AktG, which guarantees the voting right to every share, although preference shares may be issued without the voting right. For the shareholder to exercise this right, he has to have paid his contribution[281], and be present at the general meeting. If the shareholder is unable to attend the meeting he may only exercise his vote by authorising a proxy.

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277 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.57

278 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.57

279 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 122 No. 1

280 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.54

281 § 134 s.2 s.1 AktG

As the vote is a legal declaration of intention, it is possible to apply the civil-law regulations: receipt, appeal and nullity, with the consequence that a successful action to set aside could defeat the resolution.

While the execution of the voting right is voluntary for the private shareholder, institutional investors are urged to contribute. This is not only demanded by the Bundesverband Deutscher Investment- und Vermögensverwaltungs- Gesellschaften (BVI) in his Wohlverhaltensregeln[282] (Rules of Good Behaviour) but also by § 32 s.1 s.3 InvG - Investmentgesetz (Investment Act). As per this law, the investment trust should exercise the vote in the interest of its shareholders. Interestingly, the law in other countries is stronger. E.g. in the US or Spain institutional investors are oblidged to vote or France and the UK where the institutional investor has to vote or explain why he did not vote.

The scope of § 32 s.1 s.3 InvG is that the investment trusts, which could be seen as a small private shareholder for a third party account, should act independently of the custodian bank[283]. To what extent this rule is obeyed can only be estimated. Fact is that vast numbers of Kapitalanlagegesellschaften still rely on their custodians. This allows the trusts to exculpate themselves if their stocks are not voted or the vote was not in the interest of the investors, and also means they do not need to set up voting guidelines. They expect the custodian, which most often is in-house, to execute the vote with the necessary fiduciary duty. Additionally, they do not need to invest in a proxy voting service - custodian banks generally offer this service free of charge.

Again it should be emphasised that the law does not cover this practice. Only in the single case the transfer of the vote is covered. The Kapitalanlagegesellschaft must not subordinate its management to the custodian[284].

6.5.1. Voting Restrictions

The role of the Höchststimmrecht (highest voting right) was a controversial section of the articles of association. The Höchststimmrecht provided that the votes of one shareholder exceeding a certain percentage (e.g. 20%) were not counted. As a tool to prevent hostile take-overs, it has been quite common for stock corporations to limit the shares that are eligible to vote. It is probably due to this characteristic that the Höchststimmrecht was heavily criticised by the Corporate Governance Panel of the government[285].

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282 Bundesverband Investment und Asset Management e.V. (BVI) „BVI-Wohlverhaltensregeln" to download at http://www.bvi.de/downloads/INTR-5FGCK7wvr311202.pdf

283 Baur, Jürgen „Investmentgesetze" Volume 1 Berlin 1997 at KAGG § 10

284 Brinkhaus, Josef/Scherer, Peter „Gesetz über Kapitalanlagegesellschaften - Auslandinvestment-Gesetz", Munich 2003 at § 10 I No.18 (Schödermeier/Baltzer)

285 German Corporate Governance Code (amended 2003) (English Version) to download at http://www.corporate-governance-code.de/eng/download/DCG_K_E200305.pdf

However, with the introduction of the KonTraG (1998) this 'privilege' was abolished for listed companies. Now, only unlisted stock corporations are entitled to lay down Höchststimmrechte in their articles of association.
The voting restriction is implemented through an absolute maximum amount, a certain percentage of the capital stock, or a gradation of the votes. It is irrelevant whether the shareholder is a private person, a proxy or a connected enterprise. Due to § 134 s.1 s.5 AktG it is impossible to impose a restriction on single shareholders.
Although the intention of the Höchststimmrecht is primarily to serve as an alarm for hostile take-overs it undoubtedly serves further functions. As already noted, in general the structure of ownership in Germany is more concentrated and less diversified than that in the United States or the United Kingdom[286]. Therefore the Höchststimmrecht guarantees enhanced pluralism at the general meeting. Through the integration of wide sections of shareholders the minority rights are strengthened.
However, this form of decision making promotes controversial rather than constructive discussions at the AGM. It is questionable whether this is in the interests of the company[287]. Furthermore, this piece of legislation is seen to protect inefficient administrations from reform-willing shareholders. Additionally, the argument is put forward that the Höchststimmrecht can have negative effects on stock exchange rates as it lowers the chances of possible takeovers[288]. Fortunately the legislator has acknowledged the predominantly negative impact of the Höchststimmrecht and repealed it. Especially foreign capital was not really attracted as equal shareholder rights were not granted in companies which maintained the Höchststimmrecht.

In contrast to France and the Scandinavian countries, Mehrstimmrechte (multiple voting rights)[289] are not possible according to § 12 s.2 AktG. A repeal of this provision in order to get the management to pursue long-term profit maximisation would not be beneficial. Firstly, this is justified by the Equal Treatment Principle: The voting right in a stock corporation should correspond to the invested capital[290]. Secondly, especially foreign and institutional investors will be scared off. Thirdly, the capital presence in the general meetings will drop even further while accidental majorities would become more possible. Fourthly, Mehrstimmrechte in certain companies could lead to a diktat of large blockholders and would certainly be beneficial for the crossholdings network. Finally, the High Level Group of Company Law Experts[291], which was appointed by the

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286 La Porta, Rafael/Lopez-de-Silanes, Florencio/ Shleifer, Andrei/Vishny, Robert W. „Law and Finance" in Joachim Schwalbach „Corporate Governance – Essys in Honor of Horst Albach" Berlin-Heidelberg 2001 p.26-68 at p.60

287 Romano, Roberta "Less is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance" Yale Law School and National Bureau of Economic Research; Draft: October 26, 2000 p.1-78

288 Hoffmann-Becking, Michael "Münchner Handbuch des Gesellschaftsrecht – Band 4 Aktiengesellschaft" 2nd Edition Munich 1999 at § 38 No. 10 (Semler)

289 Shares with a multiple voting right have more than only one vote

290 Zöllner, Wofgang (Editor) "Kölner Kommentar zum Aktiengesetz" 2nd Edition, Cologne 1988 at § 11No.7

291 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" 2002 to download at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf

European Union, saw in the Mehrstimmrecht an obstacle for takeovers as small shareholders could easily target such offers. Hence, they support a European wide repeal of this voting right so that at least in the case of a takeover the one share – one vote principle will prevail[292].

Another point to mention is the restriction of voting rights for allocated preference shares[293]. The holders of preference shares have the same administration rights as the ordinary shareholder. They are entitled to participate in the general meeting, can take an action to set aside a resolution by the general meeting, and have the information and petition right. However, the concept of "preference" shares derives from the right to be first with the distribution of dividends. Therefore it is not surprising that the voting right is granted in cases where the preference share is concerned[294].

In addition to this, voting prohibitions are imposed on board members and certain shareholders who are personally affected by matters which are inherent in their status[295].

Restrictions are also imposed on a stock corporation holding own shares. Due to § 71 AktG it is possible for the corporation, under certain conditions, to acquire own shares, but according to § 71 b AktG the company cannot assume the rights associated with these shares. This includes voting rights and the dividend claim[296]. An attempt to evade this barring of rights using third or dependent companies is not possible. This can be compared with § 328 AktG, which restricts the rights of companies having mutual interests exceeding 25% of the total number of shares, while rights for companies with mutual interests below 25% remain untouched. However, an exception is made where the firm does not carry out its disclosure of information duty with regard to these interests[297]. An infringement will have the consequence for the company that the rights will be lost.
Violations by board members or corporations against the restrictions mentioned above could make the resolution contestable, and the offender may be fined.

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292 Wagner, Oliver for Deutsche Bank Research „EU-Übernahmerichtlinie – Erfolg nach 30 Jahren Diskussion?" 22nd May 2003, to download at www.dbresearch.de/PROD/999/PROD0000000000055473.pdf at p.5

293 § 12 s.1 s.2 AktG

294 In particular: no distribution of dividends in one year and no balance payments in the following year (§ 140 s.2 AktG); lifting or encroachment of the preference (§ 141 s.1 AktG); an introduction of further preference shares (§ 141 s.2 AktG); alteration of the articles of association, if preference shares are concerned (§ 179 s.3 AktG); capital increase, if preference shares are concerned (§ 182 s.2 AktG in conjunction with § 193 s.1 s.3, § 202 s.2 s.4, § 221 s.1 s.4 and s.3); capital decrease, if preference shares are concerned (§ 222 s.2 AktG, in combination with § 229 s.3 AktG).

295 For instance: no vote on own ratification of the acts (§ 136 s.1 AktG); no vote for ratification of acts in conjunction with a special investigation (§ 142 s.1 s.2 and 3 AktG); restriction to vote with personal liable partners in a limited partnership on shares (§ 285 s.1 AktG); questions of the management in the case of liability release or alteration (§ 119 s.2 AktG); duty to pay compensation (§ 117 AktG); assertion of claims for compensation (§ 147 AktG).

296 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.176

297 § 20 AktG, § 21 WpHG

A special act is the so-called Volkswagen Act, as it restricts proxies to the general meeting[298], with the effect that whatever will happen the state of Niedersachsen (Lower Saxony), as the major shareholder, will prevail in any proxy fight. As the German legislator is not prepared to alter this Act, the Commission of the European Union filed a suit against this practice saying it violated the Treaty of the European Union with regard to the free movement of capital (Art. 59) and the freedom of establishment (Art. 43)[299]. A ruling is pending at this point in time.

In the context of voting restrictions it is relevant to mention the possibility of voting agreements. The law (§ 136 s.2 AktG) restricts such arrangements; however, it is accepted that under certain circumstances the shareholders may commit their voting towards a third party, or the corporation. These agreements are legal.
The acknowledgement of voting agreements is only logically consistent. With regard to the fact that most of the corporate policy is not determined in the general meeting, an enhancement of legal security for the corporation often is necessary.

Finally, a ruling by the BGH[300] needs to be pointed out. According to the judgement of the court an AGM resolution does not become invalid because a shareholder was according to § 20 s.7 s.1 AktG not entitled to vote. It only becomes contestable due to an infringement of the law.

6.5.2. Proxy Voting

A crucial point of the voting right principle is the authorisation of an agent by the shareholder[301]. Proxy voting is generally possible, although the exercise of the vote via a messenger is not covered by this provision. The authorisation of credit institutes, shareholder associations and other intermediates is also possible. The provisions in the BGB - Bürgerliche Gesetzbuch (Civil Code)[302] cover the conferral of authorisation if the Stock Corporation Act (§§ 134 s.3, 135 AktG) does not state an exception.

A compelling condition for a legitimate proxy agent is the authorisation by the shareholder. Here a written notice is required. However, the NaStraG has allowed some considerable changes to this point. Although it does not waive the written form, it adopts a more flexible concordance with the regulation, by allowing other forms

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298 § 3 Gesetz über die Überführung der Anteilsrechte an der Volkswagenwerk GmbH 21.7.1960 (Act Regarding the Transition of Volkswagenwerk GmbH Shares)

299 European Commission Press Release IP/04/1209 "Free movement of capital: Commission takes Germany to the Court of Justice on Volkswagen law" 13th Oct. 2004 to download at http://www.eu.int/rapid/pressReleasesAction.do?reference=IP/04/1209&format=HTML&aged=0&language=EN&guiLanguage=en

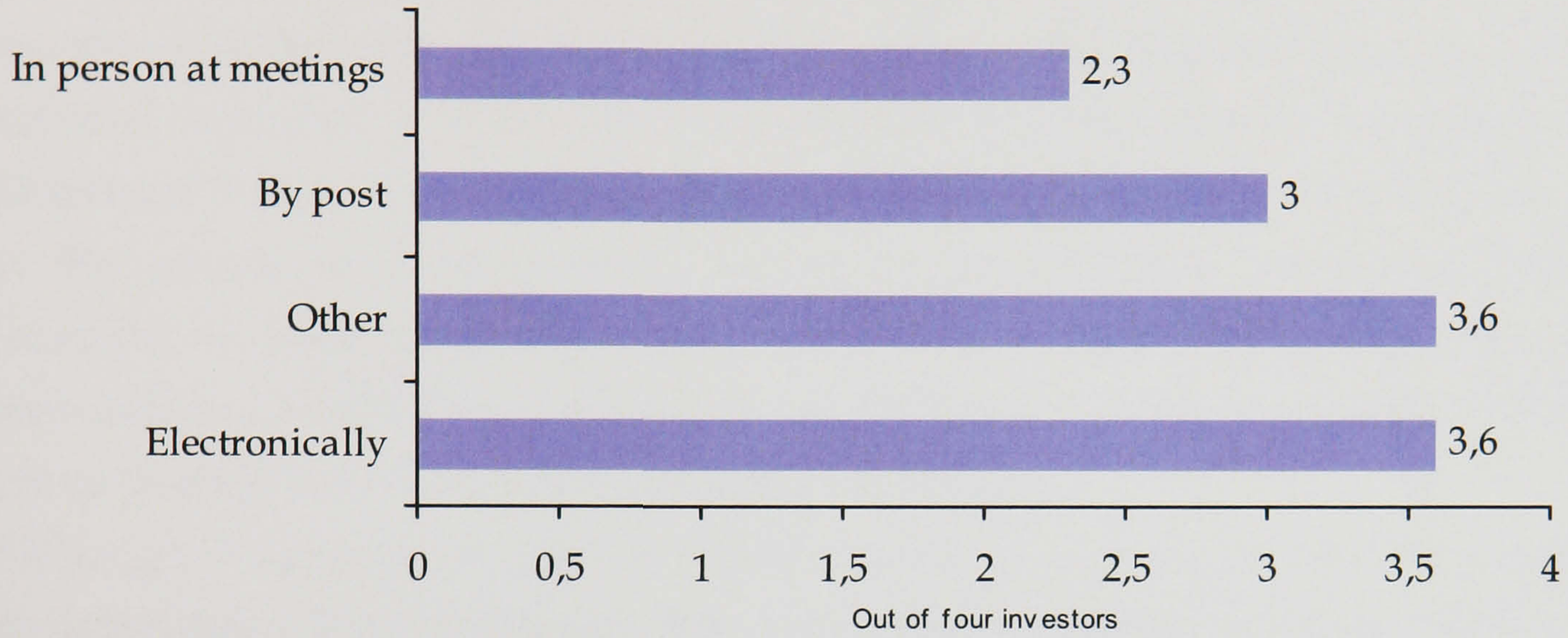
300 BGH II ZR 30/05 (24th of April 2006) at p.1

301 The determining legal provisions regarding the relation between the shareholder and the proxy are set down in §§ 134 s. 3, 135 AktG, §§ 675, 665 BGB (contract of agency).

302 §§164 - 185 BGB

including fax, e-Mail or SWIFT[303]. This provides a relative simplification of proxy voting with a number of positive consequences for the company. If implemented by the articles of association, it is not only possible for the corporation to reduce the enormous mailing and administrative costs (also derived from incoming enrolments and other administrative work) but also to simplify voting for shareholders, which would consequently enhance capital presence at general meetings.

Figure 20: Voting Methods of Institutional Investors[304]



Although this reform was made on behalf of the rediscovery of the registered share, electronic voting with bearer shares can also be executed. Here, in contrast to the registered share where the registrar has all necessary information, the entrance card of the custodian bank is decisive. As the company does not know the shareholder, it has to provide the investor with all required information.

Unfortunately, the custodian banks tend to give up their proxy voting services, rather than putting an effort into reforming their system. It would seem they are waiting on further development of the registered share, before investing in a system that allows proxy voting via the bank. Furthermore, they possibly fear spending money on a service which has produced high losses and criticism from many social groups, especially in the period following instalment.

Since 2001, a number of companies issuing registered shares have already been offering electronic voting via the Internet to shareholders. Such companies include Allianz AG, Advantec AG, Daimler-Chrysler AG, Deutsche Bank AG, Münchner Rück, Celanese AG, Telekom AG and others. So far RWE is the only company with bearer shares that offers such a service.

This development indicates that this form of shareholder service is technically and legally achievable. Although shareholder response to this offer in the first years should not be overestimated, it is expected that the adoption of the technology will increase as

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303 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Reform des Aktien- und Bilanzrechts, zu Transparenz und Publizität (Transparenz- und Publizitätsgesetz)" to download at http://www.bmj.bund.de/media/archive/301.pdf at §134 AktG

304 Grubaugh, Richard H. „Survey of Global Voting Trends" 2004 at p.14 to download at www.iirf.org (International Investors Relation Federation)

companies market the service comprehensively; Internet access grows, enabling users to get familiar with the option; and as restraints, especially from foreign investors, are overcome.

Voting via the company's webpage must be differentiated from proxy voting services (e.g. IVOX, Institutional Shareholder Services, Automatic Data Processing). Here the investor is voting via the webpage of the voting service supplier, and often follows a voting recommendation based on the agenda according to national corporate governance standards like the German Corporate Governance Code. The proxy voting service organises the distribution of the votes to the general meetings, normally via the national custodian of their clients or completely electronically, especially for the Anglo-American States. As the authorisation of the custodian is not feasible in Germany (due to the retreat of some banks), proxy voting services sometimes have to rely on alternatives. Such alternatives are: Xchanging (formerly European Transaction Bank), associations like the Deutsche Schutzvereinigung für Wertpapierbesitz (DSW), others or proxy committees, which are provided by the issuer.

Although it appears possible for corporations to pursue an electronic poll, and voting investors have the impression their vote is given directly to the company, the NaStraG still requires the physical presence of an intermediary at the General Meeting. One may have the impression that this requirement is another obstacle for the investor to make his ballot valid. However, it has paved the way legally for a new institution: the Proxy Committee. The Proxy Committee is composed of representatives of the stock corporation, often the notary who is not dependent on the company. Their only job is to accept the incoming votes and put them into the ballot box. As they do not have any freedom of choice, meaning they are not allowed to change a vote, a conflict of interest cannot arise and it is therefore legally safe[305]. However, it has to be made clear that § 665 BGB should not be valid. According to this section, the proxy has a "duty of thinking things through"[306]. To avoid conflicts of interest in the case of new petitions, or the alteration of existing ones, the proxy committee should not be allowed to vote, according to an analogous application of § 135 s.1 s.2 AktG[307].

The authorisation has to be presented to the corporation. Here again the NaStraG altered the regulation considerably. Safekeeping of the certificate of authority by the company is no longer necessary. According to § 134 s.3 s.3 AktG, it is sufficient when the company is able to verify the proxy. This reform has the undisputed advantage that administrative work is enhanced.

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305 OLG Düsseldorf "Goldzack AG" 16U 79/02 to download at http://www.justiz.nrw.de/RB/nrwe/olgs/duesseldorf/j2003/16_U_79_02urteil20030328.html at No.76

306 Hanloser, Stefan „Proxy-Voting, Remote-Voting und Online-HV: § 134 III 3 AktG nach dem NaStraG" in Neue Zeitschrift für Gesellschaftsrecht (NZG), Volume 8, 27.04.2001 p.355-358 at p.357

307 Zetzsche, Dirk "NaStraG – ein Schritt in Richtung Virtuelle Hauptversammlung für Namens- und Inhaberaktien" in Zeitschrift für Wirtschaftsrecht (ZIP), Volume 16, 20.04.2001, p.682-691 at p.684

The ability to allow a proxy to safeguard the interests of the shareholder is fundamental to maintaining stable capital presence at the general meeting, thus avoiding accidental majorities. Therefore the proxy agents play an important part in corporate policy. Not only because they enable the administration to improve their efficiency (e.g. notice to the general meeting by the custodian banks) but also because they serve as a force which the board is able to negotiate corporate issues with.

6.5.2.1. The Proxy Agent

Until the renaissance of the registered share it was the almost unrestricted privilege of the custodian banks to act as a proxy agent in general meetings. This has changed. It is now possible for the registered share-offering corporation to contact the shareholder themselves, with the result that the banks see organised proxy voting increasingly as unwelcome business[308]. Another reason is the banks having become "exceptional brokers"[309], as Noack describes. With the gradual retreat of the banks a vacuum of power has been evident. The lack of capital presence at general meetings gives proof that this issue has to be taken seriously.

Shareholders have the liberty to choose a proxy. According to the prevailing opinion, the articles of association demand certain requirements for a proxy. Therefore it is possible to stipulate that the proxy himself has to be a shareholder[310]. Nevertheless, it is accepted that the exceptions cannot enhance the exercise to vote immoderately[311].

The internal relationship between the shareholder and the proxy is determined by a contract of agency (§ 675 BGB) or if the representation is free of charge by § 662 BGB (Mandate).

6.5.2.1.1. Information Duties of the Proxy

The voting right is not only transferred because the shareholder is not able to attend the general meeting personally, but also because he expects the proxy to have expert knowledge of the issuing company and, in the case of cross-border voting, the respective financial market. Consequently, as the general meeting approaches, information and consulting duties are conferred upon the proxy.

Hence, it is uncontested that a proxy agent (lawyer, intermediary, shareholder association or other) has larger duties compared to the custodian banks. It could be alleged that they have, because of their predominant role in corporate policy, a superior

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308 The Volksbanken (cooperative banks) and the Sparkassen (savings banks) do not offer proxy voting to depositors anymore, others only on a regional, larger banks on a national, two on a global level – own research

309 Noack, Ulrich „Die internetgestützte Hauptversammlung" in Noack, Ulrich und Spindler, Gerald"Unternehmensrecht und Internet" Munich 2001 p.13-35 at p.22

310Happ, Wilhelm/Brunkhorst, Heike/Zimmermann, Norbert „Aktienrecht Handbuch – Mustertexte – Kommentar" Cologne, Berlin, Bonn, Munich 1995 at p.584

311 Ruoff, Christian "Stimmrechtsvertretung, Stimmrechtsermächtigung und Proxy-System" Munich 1999 at p. 15; Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 134 No. 26

knowledge. Therefore the prevailing opinion takes the enumeration in § 128 AktG exhaustively[312].

When the shareholder elects to confer full discretionary power upon the proxy, the latter has to execute the vote in the interest of the investor (§ 128 s.2 s.3 AktG). Since this rule does not define the voting behaviour of the proxy satisfactorily, the latter's responsibility is applied more properly when assuming that, he has to act in the interest of the average shareholder[313], with an aim to solid growth over an appropriate interest and course rate[314].

Besides information and consulting duties, the proxy also bears the responsibility of an inquiry. This is particularly the case when he intends to use the vote in an atypical and particularly venturesome manner - e.g. blocking resolutions which were instigated by the management[315].

6.5.2.1.2. The Custodian Banks

The custodian vote of the banks remains one of the most contentious issues in Company Law. This derives from a number of facts regarding the function of the banks as a credit institute, as a custodian bank and as an investment bank. This discord gives credence to the accusations of critics[316] when it comes to involvement of custodian banks in the issuer's business. The uncoupling of capital risk (granted credits, own investments) and influence potential contains the danger that the custodian votes, in doubtful cases, are not exercised in the interest of the shareholder. This is even more probable when the custodian bank has interests in the company. Here, relations between the issuing company and the custodian bank in its function as a creditor are often the stumbling block[317].

Clearly the custodian bank has conflicting interests. On the one hand it has to represent investors with the objective of increasing shareholder value (e.g. higher dividends, lower interest rates), while on the other hand they must also consider any credits given to the issuer. Their aim is a good creditworthiness (which could mean lower dividends for higher interest rates).

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312 Henssler, Martin "Verhaltenspflichten bei der Ausübung von Aktienstimmrechten durch Bevollmächtigte" in Zeitschrift für das gesamte Handels- und Wirtschaftsrecht (ZHR) Volume 157, 1993 p.91-124 at p.99

313 Geßler, Ernst/Eckardt, Ulrich/Hefermehl, Wofgang/Kropff, Bruno „Aktiengesetz" Volume II §§ 76-147, Munich 1974 at § 128 No.50 (Eckardt)

314 Wolfgang Zöllner (Editor) "Kölner Kommentar zum Aktiengesetz" 2nd Edition, Cologne 1988 at § 128 No.16

315 Henssler, Martin "Verhaltenspflichten bei der Ausübung von Aktienstimmrechten durch Bevollmächtigte" in Zeitschrift für das gesamte Handels- und Wirtschaftsrecht (ZHR) Volume 157, 1993 p.91-124 at p.101

316 Fraune, Christian „Der Einfluss institutioneller Anleger in der Hauptversammlung" Berlin 1996 from p.35ff; Schmidt, Thomas„Macht der Banken" Friedrich Ebert Stiftung, Bonn 1995 to download at http://library.fes.de/fulltext/fo-wirtschaft/00366toc.htm from p.27ff; Tuerks, Robin A."Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 from p.25ff; Hoffmann, Jochen "Systeme der Stimmrechtsvertretung in der Publikumsgesellschaft" Baden-Baden 1999 from p.23ff

317 Fraune, Christian „Der Einfluss institutioneller Anleger in der Hauptversammlung" Berlin 1996 from p.36ff

Further conflicts of interest occur during the initial public offering business. Again the bank of issue is interested in achieving high commissions, while the shareholders prefer to see easier financing terms.
Friction also arises from manpower policies as the supervisory boards usually have a number of bank representatives, leading to doubts with regard to discharges, bank financed takeovers[318] and objectivity with respect to management interweaving.
Another point of criticism arises when looking at the attitude of the custodian banks regarding their participation in voting at general meetings of weak performers, especially in the former Neuer Markt Index. Although a number of depositors decided to leave their proxies with their bank, the latter refused to work out proposals. It is assumed that the custodians feared enormous costs regarding corporate governance, bad publicity, and contributing to the total breakdown of the company. The custodian bank has to provide its own suggestions to the shareholder, per § 128 s.2 s.1 AktG, if it intends to offer proxy voting. Unfortunately, the wording of this provision is vague, allowing room for interpretation. For instance, an own suggestion could also be advice to vote according to management recommendations.
Nevertheless, in an important moment the banks refused to play their part in the corporate governance system. At general meetings of struggling start-up companies the shareholder relies on proposals by his custodian bank, which the latter does not provide. Usually, other major shareholders do not take up the initiative to cover the bank's role, and a lack of corporate governance occurs.
These arguments are emphasised by the fact that custodian banks (own shares, investment subsidiaries and custodian votes) control on average 80% of the votes at an AGM.

The banks, however, are often unfairly accused of abusing their power, when considering the number of administrated votes and their field of agitation. Apart from the proxy voting services, they are almost the only responsible and competent partners in conversations for corporate policy. Hence, they do not only function as a stabilising but also as an accidental majority-preventing factor[319]. Furthermore, because of their professional education, bankers on supervisory boards are seen as even more efficient regarding corporate governance than major shareholders[320]. Additionally, the custodian vote is often the only reasonable possibility for the holder of widely diversified shares to participate in corporate policy making.

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318 e.g. With the attempt of a hostile take-over of Thyssen AG by Krupp AG the Deutsche Bank placed consulting and capital for Krupp's disposal, although they had a member in the supervisory board of Thyssen. More detailed: Tuerks, Robin A."Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 from p.33ff

319 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.191

320 Teichmann, Christoph „Corporate Governance in Europa" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) September 2001 30.Volume number 5 p.645-679 at p.653

Given these facts it is quite surprising that custodian banks only get limited compensation for their work which does not even cover their expenses. Their payments are for covering their costs with the distribution of notifications (§ 128 s.6 No.2 AktG in conjunction with the "Decree to Compensate Expanses of Credit Institutes"), and for the distribution of additional material, e.g. quarterly reports (via an agreement between the banks and the industry). Further payments to custodian banks do not exist; there is no hidden fee in the costs for the securities account.

The proxy system with the custodian banks has a long tradition, not only the system itself but also discussion of this issue. In the reasoning of the German Stock Corporation Act 1937 it is stated:

> "Among the most disputed issues in public is the proxy vote of the custodian banks"[321].

Already in 1892 the Supreme Court of the German Reich authorised the proxy voting system[322]. Based on this decision, Hoffmann states that the banks developed a system in order to promote proxy voting in an enlarged framework[323]. With the growing economic power of the banks their influence in stock corporations increased, with accompanying criticism.

Under the Stock Corporation Act of 1937, the proxy voting system of the custodian banks was regulated for the first time. With some exceptions this draft outlines the actual Stock Corporation Act. One of the basic ideas of this regulation was to maintain the influence of small rather than large shareholders. This should guarantee equilibrium between these two fractions, which was thought to be well preserved using the proxy voting system of the custodian banks[324].

With ongoing economic recovery during the post-war period people were able to build up small but considerable assets. Again it were also the banks which were the beneficiaries of this up turn. Hence, their position in the German economy was further extended. The result was new regulations in the Stock Corporation Act of 1965[325], where the duty of information between the shareholder and the custodian bank was enhanced. Also transparency was improved and the duration of the proxy was limited to fifteen months. This discussion has received fresh impetus with the introduction of the KonTraG 1998 and the NaStraG 2001.

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321 Tuerks, Robin A."Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.1

322 Amtliche Sammlung der Entscheidungen des Reichsgerichtes in Zivilsachen (RGZ) – decisions of the supreme court in civil law Volume 30 p.51ff

323 Hoffmann, Jochen "Systeme der Stimmrechtsvertretung in der Publikumsgesellschaft" Baden-Baden 1999 at p. 23

324 Hoffmann, Jochen "Systeme der Stimmrechtsvertretung in der Publikumsgesellschaft" Baden-Baden 1999 at p. 23

325 Tuerks, Robin A."Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.1

On account of the number of votes the banks represent they have to recognise their special responsibility towards the depositor and the corporation when working out proposals. Here the KonTraG makes allowances for separating working proposals for the general meeting from own business interests; disclosure of personal and business interests with the corporation[326]; and custody scrutiny from the banking supervision[327]. In addition to that the NaStraG has repealed the duration of the proxy of fifteen months and renounced the written conferral[328].

A condition for carrying out the vote on behalf of the shareholder is the information disclosure in the lead up to a meeting and the presentation of proposals. The passing on of materials of the company for the general meeting is compulsory (bearer shares), but the bank does not have to present any proposals if it does not intend to offer proxy voting[329]. However, if a customer has own proposals to the general meeting the representing bank is obliged to act on his behalf.
An important factor in reducing intensive costs associated with the general meeting is the option to confer a substitute authorisation (§ 135 s.3 AktG). Especially with regionally active stock corporations this proceeding is even advisable, as the corporate policy might contain local aspects. In addition to that, it is possible to combine forces of different banks, shareholder associations or proxy voting agents. Nevertheless, proposals suggested previously have to be taken into account.
A point at issue is the demand of the investor to file an application[330]. Of course, the support of this shareholder right seems to be obvious when looking at the proxy voting practice of the banks. However, this approach has to be rejected. Firstly, a petitioner has to show his engagement in the corporate policy. Secondly, misunderstandings with the argumentation in the general meeting become most possible. The risk for the bank to be sued or the corporation to be met with an annulment action by an unsatisfied shareholder is too unpredictable.
Often petitions are altered during the general meeting. Here a change of the vote by the bank is still covered if it acted in the interest of the shareholder. A far narrower frame is set when the bank wants to alter its own petitions. According to § 135 s.5 AktG this is possible when new facts or occurrences have arisen so that the bank can argue that their behaviour to change their initial petition is in the interest of the shareholder. As a consequence, the credit institute has to justify its deviation from the original authority to the shareholder. There is no special formal requirement for this determined by the law. In addition to that, an offence against the interests of the shareholder is only

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326 § 128 s.2 AktG

327 § 30 s.1 s.2 KWG

328 § 135 s.2 AktG

329 Especially with the start-up companies in the (former) Neuer Markt the banks were very unobtrusive

330 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.197; Hüffer, Uwe on the "Aktiengesetz" 6th Edition Munich 2004 at § 128 No. 10

contestable internally and not towards the company. However, it is difficult, if not impossible, for the shareholder to prove that he suffered financial damage following the behaviour of the bank[331].

It is also necessary to mention the hidden proxy of the custodian banks. Under these circumstances the credit institute does not disclose the identity of the shareholder. It is sufficient to prove the authorisation.

Additionally, recent reforms of § 135 s.2 AktG, have enabled the credit institute to offer permanent authorisation requiring that it annually informs investors of the possibility of retraction or other ways to be represented (e.g. shareholder associations).

6.5.2.1.3. The Intermediaries - Towards a Global Proxy Voting and Advisory Service

Although the share of proxies financial intermediaries represent is already quite considerable[332], it can be expected that with the retreat of the custodian banks[333], their influence will increase proportionally. In future they will become the determining part in corporate policy. In this context it needs to be pointed out that an "Acting in Concert" according to § 35 s.1 s.1 WpÜG must be avoided. This paragraph binds the shareholder who has the control over the voting rights (30%) to present a takeover proposal. In a number of cases this threshold is not without the limits of a global active proxy. Hence, he needs to be aware not to give a binding vote recommendation, which is for instance the case when the investor has automated the voting process based on the policy of the proxy[334]. In a ruling[335] the BGH narrowed down the limits of acting in concert. The court stated that in the case of a supervisory board election acting in concert is not applicable. Similarly the Oberlandesgericht Frankfurt[336] decided that the conditions for acting in concert are only met when a conscious practiced collaboration is given.

Other factors than the retreat of the custodians also foster the growth in importance of the intermediates[337]. Firstly, they can promote their service independently. Especially Anglo-American investors assess this point as significant. This assumption is reinforced by the relatively poor capital presence in general meetings of companies with a high share of foreign investors[338]. Therefore it is probable that the proxy voting service will adjust itself internationally, which will give it the best possible utilisation of its customers' holdings.

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331 Very comprehensive on the internal relation between the custodian bank and the depot customer: Busse, Andreas „Depotstimmrecht der Banken" Wiesbaden 1962 p.87-96

332 e.g. Proxies represented by ISS at the 2004 AGM of Siemens: 20,4% of the capital being present

333 Noack, Ulrich/Spindler, Gerald"Unternehmensrecht und Internet" Munich 2001 at p.22

334 Schneider, Uwe H./Anziger, Heribert M. „Institutionelle Stimmrechtsberatung und Stimmrechtsvertretung - „A quit guru's enormous clout" in Neue Zeitschrift für Gesellschaftsrecht (NZG), No.3, 2007 pp.88-96 at p. 93

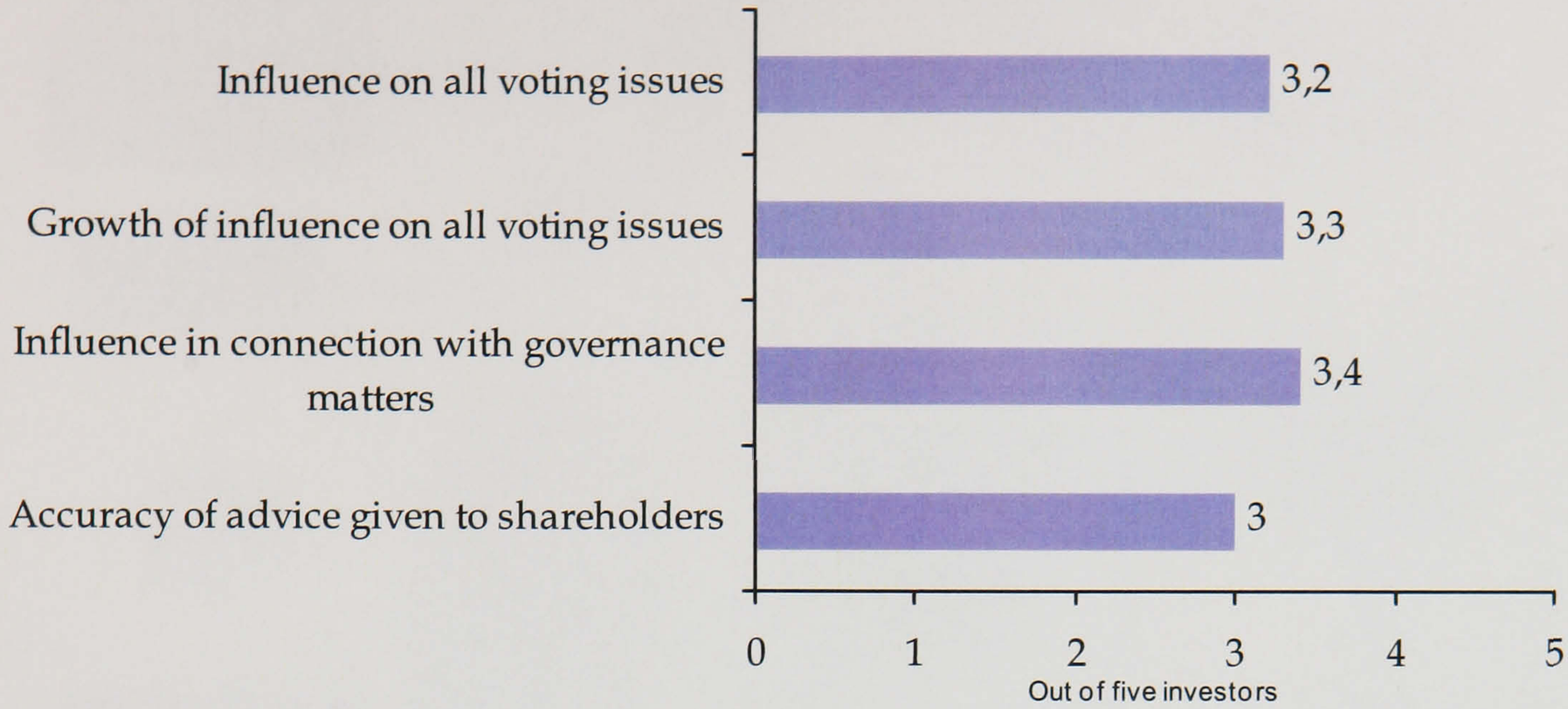
335 BGH II ZR 137/05

336 OLG Frankfurt a. M. Az. WpÜG 5/03a (25.06.2004) in to download at http://www.hefam.de/urt20/WPUEG503A.html

337 Juschus, Alexander - Working Paper for the Finance Committee of the German Parliament "Standards für Finanzintermediäre" 2002 at p.4

338 See Figure 29: Shareholder Structure of Selected Stock Corporations 2004

Figure 21: Institutional Investors on the Influence and Accuracy of Proxy Advisory Firms[339]



These voting services are capable of concentrating on a target group. As they do not need to represent every private shareholder like the custodian banks, they can serve institutional and corporate investors exceptionally well[340]. This does not only enhance their effectiveness but also improves investor relations. Moreover, with the integration of other services like class action tracking, vote disclosure, voting results, corporate governance rating, or most importantly, voting recommendations, they can represent themselves as the omnipotent corporate governance service. Consequently, they are not only capable of functioning as a balance to the custodian banks, but of superseding them in a number of fields with respect to corporate action.

Voting services generate the ballots for the general meeting from the information they receive from the custodian, the investment company, the issuer, or from official sources like the Bundesanzeiger in Germany. Having received the necessary data, they customise it for each client and transfer it to the voting platform. The person who is entitled to vote, usually the fund manager, now views not only the agenda of the meeting on his screen but also his holdings, and if available, voting recommendations or research. He may cast his vote and send it to the proxy voting service. The latter puts it in an accepted ballot format (most often Email or SWIFT) and distributes the votes electronically via ADP or comparable systems, custodian banks and other intermediaries (e.g. registrar), or proxy committees, to the general meetings. The fund manager subsequently receives the information that his vote has been delivered successfully.

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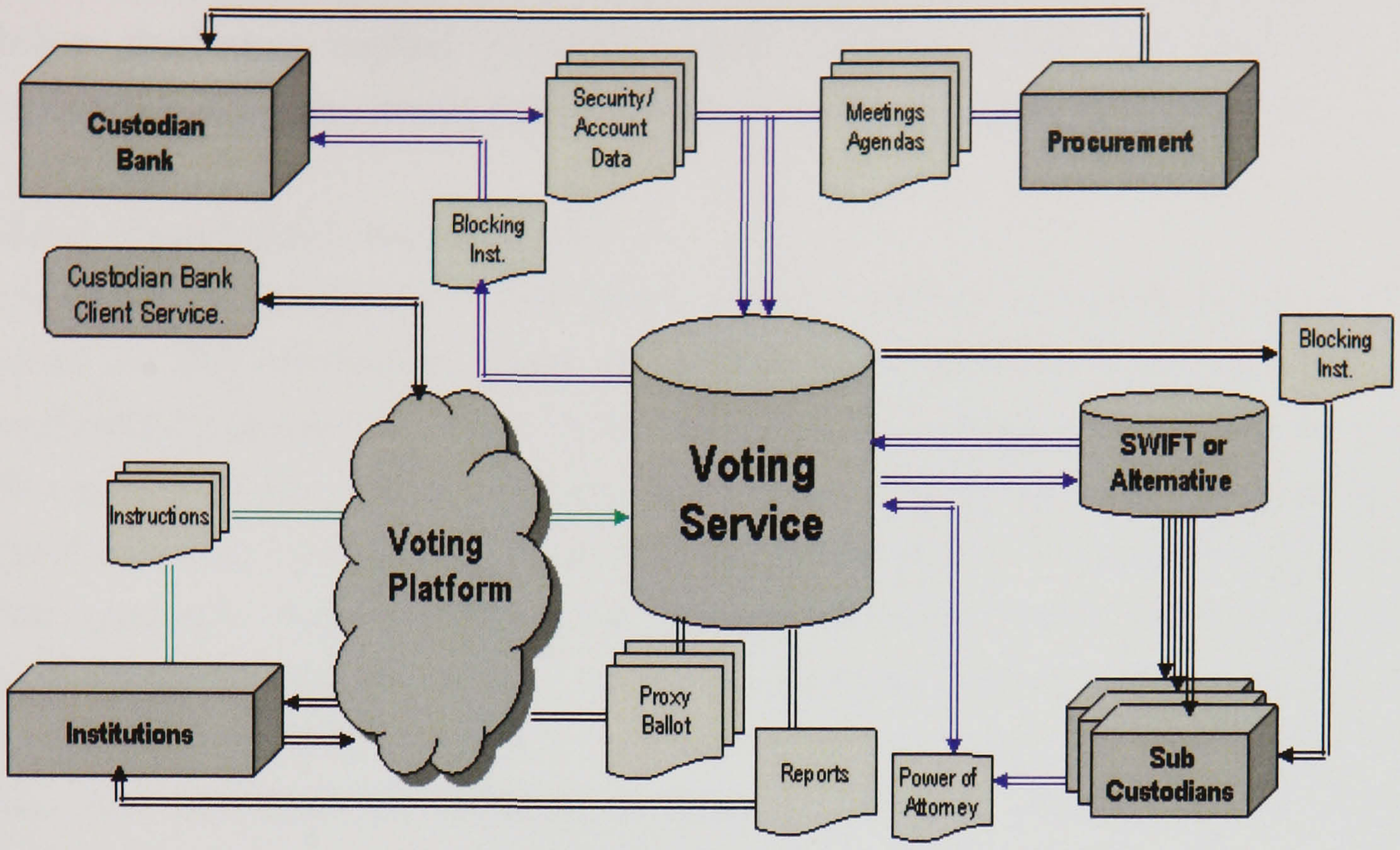
339 Grubaugh, Richard H. „Survey of Global Voting Trends" 2004 at p.9 to download at www.iirf.org (International Investors Relation Federation)

340 Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance" Baden-Baden 1999 at p.73

Figure 22: Tasks Taken over from a Custodian by a Proxy Voting Service[341]



In contrast to the custodian bank the legal ground of the intermediate is exclusively based on the contract of agency according to §§ 675, 665 BGB.

A crucial point for the intermediate is the question of finance. As the intermediate cannot raise custodian fees and will also not receive refunds for the distribution of the materials for the general meeting, he is dependent on other sources.

Two possibilities are likely. Firstly, the intermediate can raise a charge towards the company, which depends on the amount of the votes handed in. It should be pointed out that, unfortunately, such a solution implies the risk of a conflict of interest where the intermediate also offers voting recommendations.

Alternatively the investor pays the intermediate. As he cannot expect to represent private shareholders, they have to receive compensation from institutional shareholders. This system has the advantage that the intermediate does not need to be concerned with national characteristic features with regard to Company Law. Additionally, the group of institutional investors would be more open to other products, like corporate governance analysis, corporate governance ratings or publication services. Under this method the intermediate would avoid any accusations of a conflict of interest. Due to § 135 s.9 AktG the proxy acts permanently for the investor.

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341 GPD (Global Proxy Distribution) selling document from Institutional Shareholder Services

This figure shows the tasks taken over from a custodian by a proxy voting service. The first task is the procurement work (all meeting information and relevant holdings of the investor), which is described on the top. This information is provided to the institutional investor via the voting platform (bottom left). The institution instructs the voting service via the electronic voting platform. When this has happened the voting service sends blocking instructions to the custodian, respectively subcustodians. The vote is send to the relevant custodian. Finally a report is produced that the vote has been delivered according to the shareholder's instruction (bottom center).

In summary, although the developing business of the intermediaries/proxy agents is capable of countering the dominance of the custodian banks internationally, and may stabilise declining capital presence, their existence will rise and fall with their acceptance among the institutional investors and with the costs involved.

6.5.2.1.4. Shareholder Associations

Shareholder associations[342] also offer proxy voting to shareholders. However, in contrast to the enormous share of proxies with custodian banks, their fraction is considerably modest[343] with less than one percent (excluding employee associations). Although their influence on a ballot basis seems negligible, their role, especially in the general meeting, has to be assessed as being substantial. In general, legitimate criticism of the company respectively the management board is mostly generated through these shareholder associations as well as fund managers. Depending on the interest group they are representing, they make contributions to topics like increasing shareholder value, the situation of women in the corporation, environmental activities and recruitment policies towards handicapped persons. However, as they are associations for special interest groups and are not geared solely towards an economic existence, it is to be expected that their share with proxies will not increase.

6.5.2.1.5. Employee Shareholders

Another point to put into perspective is the interest of employees' shares in certain companies[344]. As they are in a position to form an association for the general meeting, their influence could be remarkable. Thus, they could be a serious opposition towards the management. For instance the Deutsche Bank has employee shareholders worth 11%, while the overall employee numbers at the general meeting is more than 30%. Hence, the perfect association of Deutsche Bank employees could be able to block important decisions by the management. Unfortunately, most of the employees have their shares in the custody of a bank, which offers special conditions for employees of certain companies (e.g. no charge for the custody of Daimler-Chrysler employee shareholders at the Deutsche Bank). Consequently, the proxies are also given to the bank or the vote is simply not executed.

According to § 135 s.9 No.1 AktG the period of the proxy is conditionally permanent.

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342 e.g. Deutsche Schutzvereinigung für Wertpapierbesitz (German Protective Association for the Possession of Securities) at www.dsw-info.de

343 Tuerks, Robin A."Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.26

344 see Figure 29: Shareholder Structure of Selected Stock Corporations 2004

6.5.2.1.6. Other Intermediaries

Other intermediaries include lawyers, tax accountants and private individuals. In general they act for a small number of larger investors. Nevertheless, as they rarely work out proposals they could rather be assessed as being messengers. Regarding the fact that they do not offer proxy voting on a commercial basis (it cannot be assumed that lawyers or tax accountants offer proxy voting as business) the proxy is delegated to them only for a single case and not permanently.

6.5.2.1.7. The Problem with the Dependant Proxy Committee

A point at issue is the role of Proxy Committees[345] who are dependent on the stock corporation. Their job is to accept incoming votes, in the form of fax, E-mail, SWIFT message, the companies' own online voting system, or whatever the issuer's articles of association provides, and places them into the ballot box. Thus, they function as the extended arm of investors who are not able to attend the meeting personally or cannot send a representative, but have, or feel, the obligation to vote. Generally the proxy committee consists of members of the investor relations departments, Company Lawyers, but mostly notaries[346]. It must not contain members of the management.

The prevalent opinion of the literature, including Hüffer and Zöllner, pleads that a representation of votes by the stock corporation or its executive body is not possible[347]. This is also valid for a company established to accept proxies[348]. This derives from an exemption, which is made by § 135 s.1 s.2 AktG, that the custodian bank is allowed to carry out the proxy in its own general meeting. Prohibition would bear the danger that competing custodian banks could push through uncomfortable decisions. Regarding this exception it has to be assumed that the legislator intended to ban any self-representation, which is contrary to the understanding of corporate governance. Even if the scope of the proxy was limited to the utmost, still a danger of abuse would exist. Representation by a certain member of the corporation[349] is judged differently. Here the opinions are unanimous, if the delegation concerns only isolated cases.

Nevertheless, particularly since the introduction of online voting via the company's web page, discussion has been rife. A number of issuers offering this service to their

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345 Recommended by the Deutscher Corporate Governance Kodex to download at http://www.corporate-governance-code.de/eng/download/DCG_K_E200305.pdf at 2.3.3 (English Version)

346 The role of the notary is comprehensively described by: OLG Düsseldorf "Goldzack AG" 16U 79/02 to download at http://www.justiz.nrw.de/RB/nrwe/olgs/duesseldorf/j2003/16_U_79_02urteil20030328.html

347 Hüffer, Uwe on the "Aktiengesetz" 6th Edition Munich 2004 at § 13 No.25; Zöllner, Wolfgang (Editor) in "Kölner Kommentar zum Aktiengesetz" 2nd Edition, Cologne 1988 at § 135 No.73; other opinion LG Stuttgart in Die Aktiengesellschaft (AG) 1974 at p.260

348 LG Baden-Baden in Zeitschrift für Wirtschaftsrecht (ZIP) 1998 p.1308-1313 at p.1310; OLG Karlsruhe Zeitschrift für Wirtschaftsrecht (ZIP) 1999 p.750-754 at p.750

349 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 13 No.25; Hoffmann, Jochen "Systeme der Stimmrechtsvertretung in der Publikumsgesellschaft" Baden-Baden 1999 at p.77

shareholders put in a representative who accepted the online votes and deposited them in the ballot box[350]. This issue is crucial as, on the one hand the NaStraG demands a representative at the general meeting, and on the other hand this procedure comes close to the representation of the company or its executive body mentioned above. However, this concept is actually a courier service rather than proxy representation. The shareholder votes on his screen by clicking a number of buttons before he sends his explicit vote to the server of the company (Fax or hard copy proxy card are also an option). Hence, the representative has no influence over the vote for his own or other reasons. Unfortunately, the institution of a messenger is not possible in Company Law[351], yet the company has almost no other choice. If it decides to appoint a third person the problem of an inadmissible representative will occur. However, as Noack and Spindler recognise the danger of a self-representation, self-control is not topical with this constitution[352]. Therefore there is no reason to prohibit this proxy voting system, as long as the representative has no decision right.

Since the introduction of the proxy committee, it proved to be a successful tool to encounter the decreasing interest in voting. Now it is discussed to make the introduction of an independent proxy committee legally compulsory[353] and not to leave it dispositive to the statutes of the company.
Yet to be settled is the question of the period over which the proxy is assigned to the representative. To protect the interests of the shareholder the authorisation should only be valid for a single vote. As the Stock Corporation Act does not state a position on this issue, it is argued that due to the period required in § 134 s.3 s.3 AktG, the legislator acknowledges the proxy only for the single case[354]. This is also valid for proxies appointed by the company, although they might be subjected to § 135 s.9 AktG. This is a logical consequence. It would be implausible to say on the one side that proxy voting via the company's administration is only legally incontestable in the case of an explicit proxy and on the other side to accept it durably.

6.5.2.2. Questions of Liability in the Shareholder – Proxy Relationship

In the first instance it is important to mention that the investor does not have the right to file an appeal against resolutions, according to § 243 s.1 and s.2 AktG, which arose because the proxy breached his duty of the internal relationship with the shareholder[355].

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350 e.g. Deutsche Bank AG, DaimlerChrysler AG, Deutsche Telekom AG

351 Noack, Ulrich/Spindler, Gerald "Unternehmensrecht und Internet" Munich 2001 at p.22

352 Noack, Ulrich/Spindler, Gerald "Unternehmensrecht und Internet" Munich 2001 at p.25

353 Klühs, Hannes „Präsenzboni für die Teilnahme an der Hauptversammlung – Ein Vorschlag zur Steigerung der Hauptversammlungspräsenz bei Aktiengesellschaften" 2005; Paper No.124 to download at http://publikationen.ub.uni-frankfurt.de/volltexte/2005/2335/pdf/124Aufsatz_prn.pdf at p.2

354 Noack, Ulrich „Stimmrechtsvertretung in der Hauptversammlung nach NaStraG" in Zeitschrift für Wirtschaftsrecht (ZIP) 2001 p.57-63 at p.62

355 Tuerks, Robin „Depotstimmrecht versus US.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p. 13

This is emphasised by the requirement that only shareholders stating their protest while attending the general meeting in person, are entitled to take this course of law (§ 245 No.1 AktG)[356].
Having said that, it has to be mentioned that with regard to the question of liability in the shareholder-proxy relationship two possibilities are provided by the law: contractual and offence. The great difficulty for the shareholder is not only to assert damage but also to show the causality and the infringement of interest[357]. While the small private shareholder will probably struggle to assert damage because the custodian bank or shareholder association did not vote according to his instruction, the institutional or major investor will probably have difficulties to show that his proxy infringed his interest. This derives from the assumption that the latter had a good reason not to follow the instruction and covered himself as the voting approached.

According to Kropff, the liability of the credit institute stated in § 135 s.11 AktG, has more of an academic background, and should prevent an exclusion in the custodians' general terms and conditions (not in those of the associations and others) [358].
Nevertheless, a proxy infringement by a custodian bank could be treated as an administrative offence[359] and pursued by the banking supervision. Accordingly, it should be mentioned that an administrative consequence of infringing a proxy by an intermediate is a dilemma yet to be solved.

6.5.2.2.1. Contractual Liability
However, the shareholder might seek compensation based on contractual liability. This right is granted to the investor in § 280 s.1 BGB. The problems he will face have been stated above, and it is generally thought to be extremely difficult for the shareholder to succeed on this course of law against the proxy[360].

6.5.2.2.2. Liability out of an Offence
Another possibility is to make the proxy liable because of an offence. Here the shareholder could assert compensation according to § 823 II BGB, which states that the proxy must have infringed a protective law. Whether § 135 AktG is such a protective law is a point at issue[361]. The question is where does this provision have a protective

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356 Hoffmann-Becking, Michael „Münchner Handbuch des Gesellschaftsrechts" Volume 4 - Aktiengesellschaft, 2nd Edition, Munich 1999 at § 39 No.62

357 Geßler, Ernst/Eckardt, Ulrich/Hefermehl, Wofgang/Kropff, Bruno „Aktiengesetz" Volume II §§ 76-147, Munich 1974 at § 135 No.131 (Eckardt)

358 Geßler, Ernst/Eckardt, Ulrich/Hefermehl, Wofgang/Kropff, Bruno „Aktiengesetz" Volume II §§ 76-147, Munich 1974 at § 135 No.132 (Eckardt)

359 § 405 s.3 No.4 and 5 AktG

360 A research did not show any rulings, which indicate that a suit has been filed on conditions yet.

361 In support of § 135 AktG as a protective law:
Geßler, Ernst/Eckardt, Ulrich/Hefermehl, Wofgang/Kropff, Bruno „Aktiengesetz" Volume II §§ 76-147, Munich 1974 at § 135 No.131 (Eckardt), Tuerks, Robin „Depotstimmrecht versus US.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p. 14
Against: „J. von Staudingers Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetz und Nebengesetzen", Second Book - Law of Obligations §§ 823-825, Thirteenth Revision 1999 by Hager, Johannes at § 823 G43

feature[362] justifying a compensation case following its violation? The discussion is left open since, because of the difficulties mentioned above it would only be of theoretical nature.

A further possibility to make the proxy liable could be through § 826 BGB. Condition in this case is that the proxy has intentionally caused an immoral damage. This is for instance the case when the proxy has approvingly accepted impairment of the represented shareholders.

For good reason the legislator repealed UMAG § 117 s.7 No.1 AktG, which provided that the shareholder was not liable to compensate the damage he caused with the execution of his vote. This norm was interpreted restrictively, as in severe cases, § 826 BGB is applicable[363].

The Federal High Court ruled that an offence against good customs (according to § 826 BGB) is made when the execution of the vote bears no relation to the purpose. This approach is heavily criticised as being too restrictive[364] as it might lead to punishing minority shareholders, which cannot be the idea of the legislation. The voting conduct should be determined by entrepreneurial thinking, which naturally includes certain risks, rather than by addressing the question of potential liability.

6.5.2.3. Liability towards Third Party Shareholders[365]

It is also true that the instructing shareholder and his proxy are liable towards third party shareholders.

The third party shareholder is in the first instance dependent on an appeal against the resolution[366] he intends to challenge. Hence, the mentioned liability provisions are secondary courses of action.

The represented investor might be liable (via § 280 s.1 BGB) towards third party shareholders because he instructed his proxy and used him as a vicarious agent (§ 278 BGB)[367], subject to the condition that the proxy has caused a damage in fulfilment of his obligation to his investor. Liability could also be accepted if the shareholder has to take the responsibility for culpable impossibility.

However, most probably the investor will have difficulties proving that he has suffered damage.

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362 This assumption is also supported by the BGH in „Der Betrieb" (DB) 1992 p.1673ff

363 „J. von Staudingers Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetz und Nebengesetzen", Second Book - Law of Obligations §§ 826-829, Thirteenth Revision 1998 by Oechsler, Jürgen at § 826 No.282

364 „J. von Staudingers Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetz und Nebengesetzen", Second Book - Law of Obligations §§ 826-829, Thirteenth Revision 1998 by Oechsler, Jürgen at § 826 No.288; Henssler, Martin "Verhaltenspflichten bei der Ausübung von Aktienstimmrechten durch Bevollmächtigte" in Zeitschrift für das gesamte Handels- und Wirtschaftsrecht (ZHR) Volume 157, 1993 p.91-124 at p.123f

365 Shareholders, which are outside the contractual proxy-shareholder relationship

366 § 243 s.1 AktG

367 Henssler, Martin "Verhaltenspflichten bei der Ausübung von Aktienstimmrechten durch Bevollmächtigte" in ZHR Zeitschrift für das gesamte Handels- und Wirtschaftsrecht Volume 157, 1993 p.91-124 at p.111

The BGH (Federal High Court) also did not accept a liability in the Law of Obligations of the proxy towards third party shareholders. Only if the proxy used his voting right "für den, den es angeht" (for that party, whose concern it is) and he did not reveal the principal, is he liable via § 179 s.1 BGB[368].
Finally, liability through a breach of § 826 BGB, covered under 'The Questions of Liability in the Shareholder – Proxy Relationship" may be used by third party shareholders. However, in this respect it is necessary to mention that professional liability does not exist, as Henssler points out[369].

As a result, the conclusion which must be drawn is that infringement of a proxy is only sanctioned in the area of an administrative offence and breach of loyalty. The sanction between the shareholder and his representative is only of theoretical nature.

6.5.2.4. Validity of the Vote

Once the proxy has given his vote contrary to the agreements with the shareholder, the question arises whether this vote is still valid. For reasons of legal security this has to be answered in the affirmative[370]. It would not be comprehensible to make resolutions of the general meeting contestable because of deficiencies in the relationship between the shareholder and his proxy, which, in addition, are not in the sphere of influence of the company[371]. This detail was recognised by the legislator, who did not acknowledge the power of contestability for the shareholder in § 245 AktG. The last option for the investor (or a third party) would only be to file a contradiction in the general meeting. However, a shareholder who authorises a proxy will probably not obtain information about his behaviour before the end of the meeting. The legal requirements are aggravated by the prerequisite that the vote had to be decisive for the resolution to be accepted.
The same is valid for shortcomings with legal justifications. If the proxy votes without being authorised by the shareholder, the latter is only entitled to file an action when he, or a third party, files a contradiction against the resolution.

6.5.2.5. Conclusion of the Proxy Agent Issue

As a conclusion it would be extremely interesting to trace the developments of the proxy agent sector. With the retreat of the custodian banks it is probable that commercial intermediates will fill the gap. Since they are in the position to act

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368 Bundesgerichtshof (Federal High Court), Ruling from 20.03.1995 – II ZR 205/94

369 Henssler, Martin "Verhaltenspflichten bei der Ausübung von Aktienstimmrechten durch Bevollmächtigte" in ZHR Zeitschrift für das gesamte Handels- und Wirtschaftsrecht Volume 157, 1993 p.91-124 at p.122f

370 Ruoff, Christian: "Stimmrechtsvertretung, Stimmrechtsermächtigung und Proxy-System" Munich 1999 at p. 54

371 Hoffmann-Becking, Michael "Münchner Handbuch des Gesellschaftsrecht – Band 4 Aktiengesellschaft" 2nd Edition Munich 1999 at § 38 No.62 (Semler)

efficiently and hence more profitable, intermediates could become a force to be reckoned with. Naturally, it is essential for them to solve the problem of financing, and to gain the confidence of both stock corporations and investors to become successful players.

Ongoing globalisation will also have impacts. Hopefully, the EU-Commission's Action Plan on modernising Company Law and enhancing corporate governance and the resulting Directive will set necessary standards for the member states, as the issue of the proxy voting agent is capable of improving corporate governance and the control and quality of international capital flow.

6.5.3. Aspects of Cross-Border Voting

With regard to capital presence in general meetings it is peculiar that although foreign investors' interest is considerable for shares, especially in the DAX (e.g. 2004: Adidas 84%, Deutsche Börse 2004: 59% - 2005: 77%)[372], the rights that accompany the property of the shares seem rarely to be practised. Figures 23 (German institutional investors) and 24 (global institutional investors) offer prove for this phenomenon.

Figure 23: German Kapitalanlagegesellschaften which Safeguard their Cross-Border Voting Right[373]

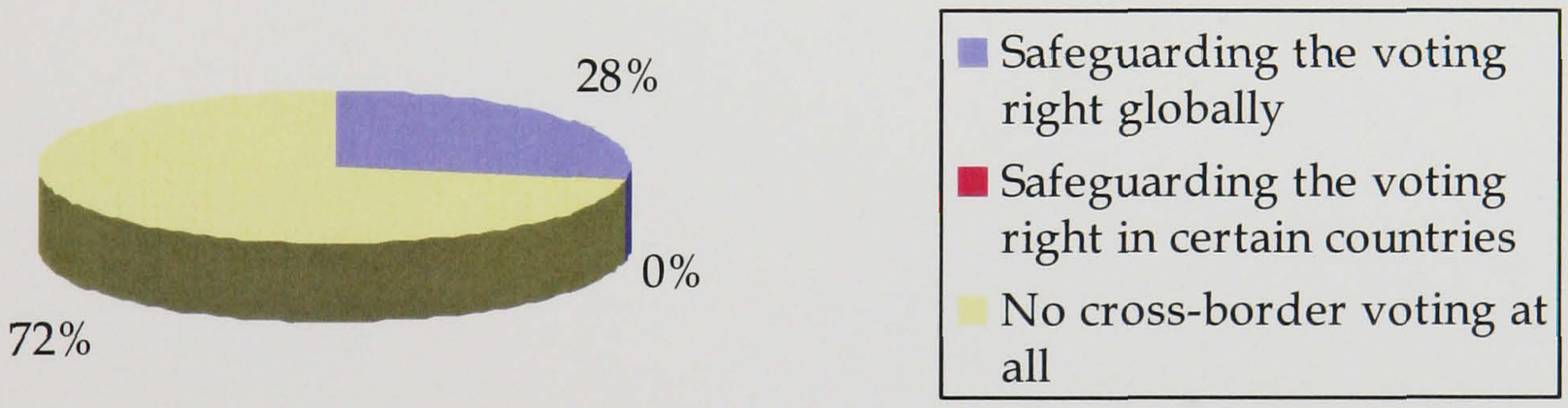
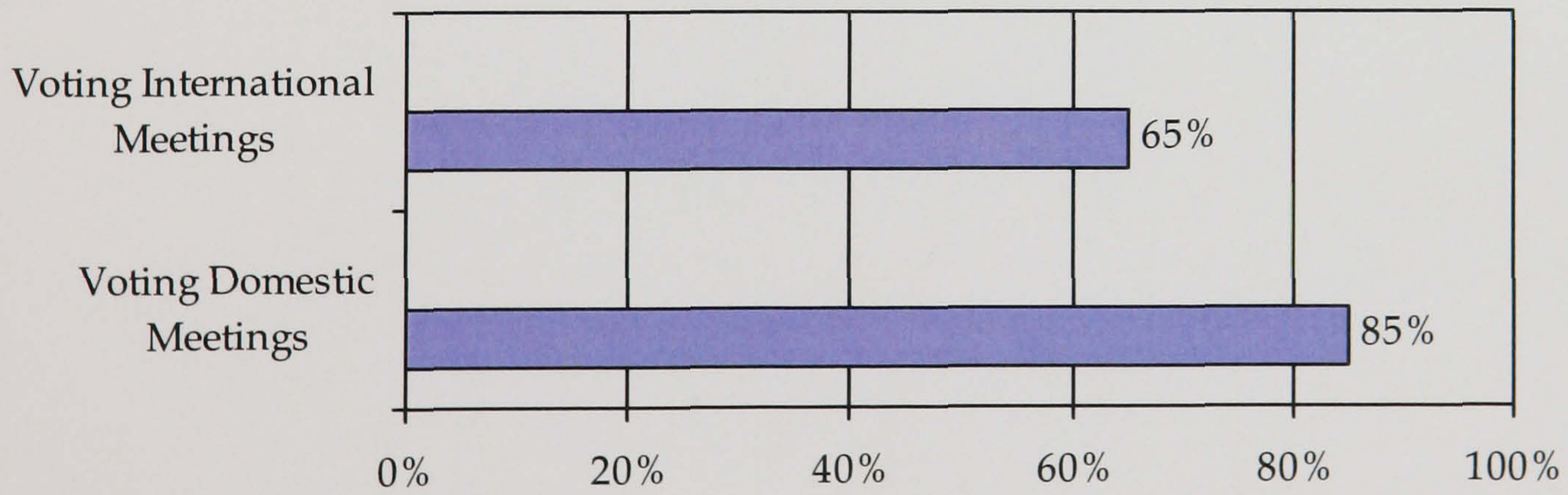


Figure 24: Global Institutional Investors which Safeguard their Voting Right[374]



372 see Figure 29: Shareholder Structure of Selected Stock Corporations 2004

373 Survey of the DSW – Deutsche Schutzvereinigung für Wertpapierbesitz among German Kapitalanlagegesellschaften, 2004 to download at www.dsw-info.de/DSW-Fondsumfrage.442.0.html#698

374 Grubaugh, Richard H. „Survey of Global Voting Trends" 2004 at p.32 to download at www.iirf.org (International Investors Relation Federation)

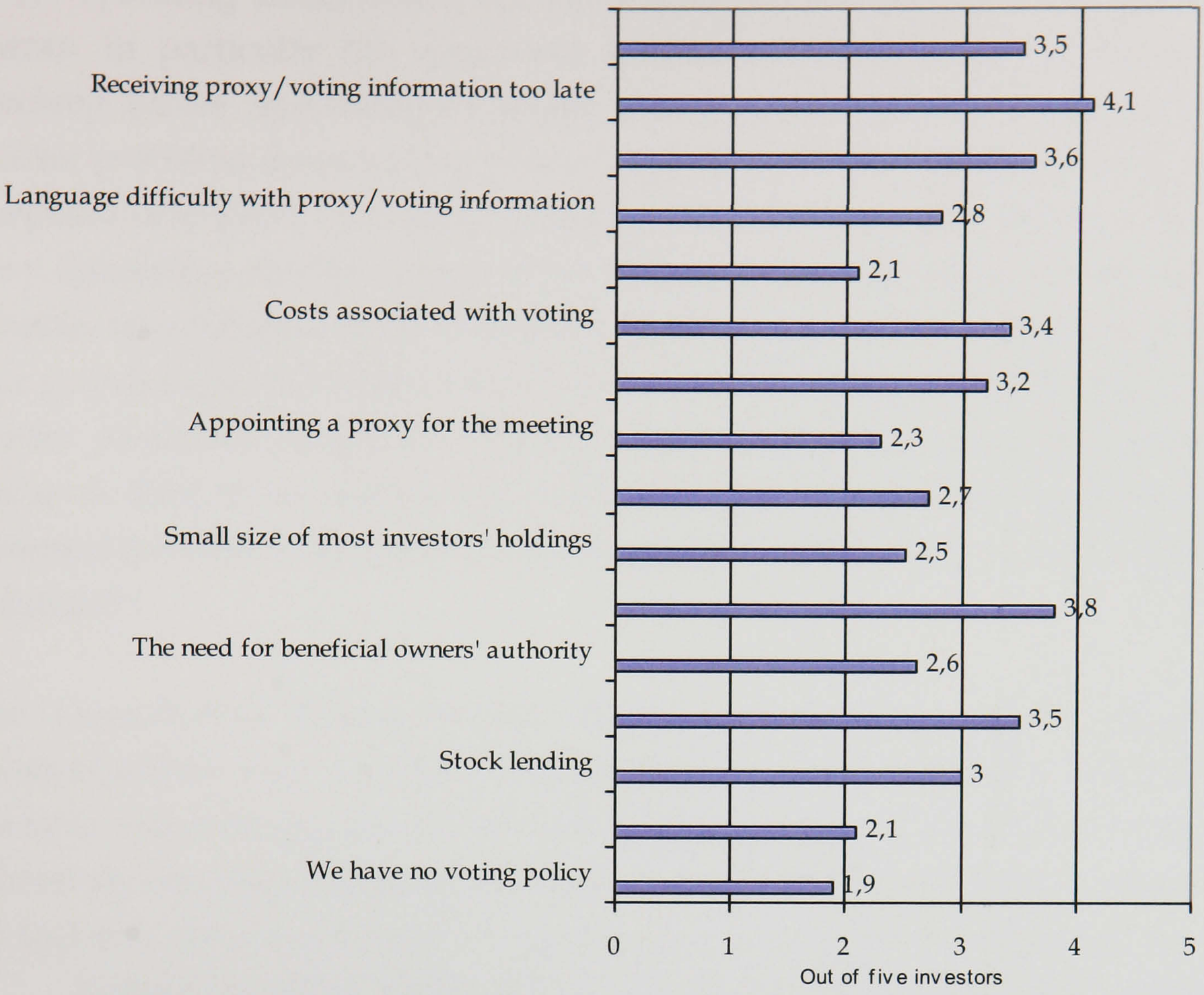
There are a number of reasons for this trend. First, the vast amount of different regulations[375] can be identified. Although numerous markets make considerable efforts to make voting easier still the variety of rules serves as an excuse. (E.g. Blocking and record date markets, requirement of re-registration of the shares prior to the meeting) Furthermore, the insufficient flow of information between custodians, investment funds or other institutions could make voting more difficult as well. Still, especially small stock corporations only provide AGM material in the local language.

In Germany, it could also be assumed that investors see voting more as a necessary evil (and consequently keep it on a minimum) rather than an opportunity to promote fiduciary responsibility or to express satisfaction and dissatisfaction with the management of the company.
Figure 25 provides prove for this assumption by pointing out the shortcomings in detail.

In any case, it is astonishing that stock jobbing takes a practically normal course, while shareholder rights give the investor a number of problems.

375 The vast variety of different legal systems in the EU is presented in Baums, Theodor "Shareholder Representation and Proxy Voting in the European Union" in Hopt/Wymeersch "Comperative Corporate Governance" 1997 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm

Figure 25: Obstacles for Executing the Cross-Border Voting Right[376]



As the title suggests, cross border voting describes action of voting rights of the global shareholder, without national barriers.
In a first step the European Union had therefore introduced an Expert Group on Company Law, which also investigated aspects of Cross-Border Voting, chaired by Jaap Winter (Henceforth "The Winter Committee")[377], to suggest methods of harmonising the systems. In addition to that a special Cross-Border Voting Group has conducted its own consultation process and presented its final report in September 2002[378].

The suggestions made by the EU Expert Group were picked up by the EU-Commission, with the consequence that an action plan on modernising Company Law and enhancing corporate governance was drawn. This Plan should be understood as the preparation for an EU- directive[379].

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376 Grubaugh, Richard H. „Survey of Global Voting Trends" 2004 at p.33 to download at www.iirf.org (International Investors Relations Federation)

377 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" (2002) at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf

378 Expert Group on Cross-Border Voting "Consultative Document on Cross-Border Voting in Europe" 2002 to download at http://www.ministerievanjustitie.nl:8080/B_ORGAN/wodc/reports/crossb.htm

379 European Commission – Directorate General Internal Market „Fostering an Appropriate Regime for Shareholders'Rights" 2004 to download at http://europa.eu.int/comm/internal_market/company/shareholders/ consultation_en.pdf at p.5

In contrast to a number of stock corporations, the EU Expert Group found that market forces operating alone would not address or remedy problems experienced in voting shares. In particular the committee scrutinised possibilities in the areas of share blocking before up-coming meetings; differing settlement periods; issues of lending shares; problems surrounding privacy; questions of the beneficial voter for regulatory purposes; and direct communication between issuer and shareholder. The latter area is very interesting for the future of the bearer share especially, as the committee asks whether two different types of shares are still opportune in a common market.
Not surprisingly, the High Level Group of Company Law Experts found that in cross-border situations, shares are typically held through chains of intermediaries, which makes it difficult to identify the person entitled to vote. Often cross-border voting is almost impossible in practice, yet the integration of financial markets calls for an urgent solution[380].

The Cross-Border Voting Group recommends that the rights and obligations of accountholders and securities intermediaries in the securities holding systems in Member States be regulated at EU level to ensure that accountholders across the EU can effectively exercise voting rights on shares they hold through these systems.
To that end, the Cross-Border Voting Group basically recommends that "accountholders in

> European securities holding systems, who are not participating in these systems as securities intermediaries holding shares for their accountholders (such accountholders are defined as "Ultimate Accountholders" in the Final Report of the Cross-Border Voting Group), should be acknowledged across the EU to have the right to determine how to vote on shares they hold in their accounts (the primary rule). An ultimate accountholder should be granted the options available under the law of the member state of the company in which he holds shares to be either recognised as the formal shareholder entitled to vote, or to receive a power of attorney from the securities intermediary who is formally entitled to vote, or to instruct that securities intermediary to vote according to his instructions. Securities intermediaries are to be prohibited from voting on shares they hold for their accountholders, unless explicitly instructed or authorised by their accountholders.
> Where an ultimate accountholder is not a securities intermediary in the regulated European securities holding systems, but nonetheless holds shares on behalf of third parties (e.g. a US securities intermediary), such an ultimate accountholder should be able to designate its clients to be recognised as entitled to determine how the shares are voted (the supplementary rule)[381]."

Additionally, the High Level Group of Experts emphasises that:

> "A proper system for shareholder information, communication and decision-making in Europe facilitates the exercise of voting rights of all shareholders in European listed companies, regardless of the member state in which they are located and whether they wish to vote on shares

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380 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" (2002) to download at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf at p.8

381 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" (2002) to download at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf at p.54

> of companies in their own jurisdiction or in another jurisdiction. It is also important that such a system allows shareholders outside the EU to exercise their rights efficiently, as the Cross-Border Voting Group has recommended through the combination of the proposed primary and supplementary rule. Finally, such a system should operate efficiently for all parties concerned: shareholders, listed companies and securities intermediaries, with respect to both administrative and operational burdens and costs. Modern technology can be highly instrumental in achieving these ends and its use by all parties concerned should be stimulated to the maximum[382]."

In summary, the Cross-Border Voting Group as well as the High Level Group sees the issue of cross-border voting as a key priority for modernising Company Law in the European Union.

Regarding the increasing institutionalisation of the entire international capital markets, it is worth considering whether intermediates could become a prism capable of compensating for shortcomings of the different legal systems. With respect to voting, especially for proxy voting services, adjustment to local market requirements is essential to carry out business. Enhancing the role of globally operating intermediates might be a solution beyond the European Union. Especially with respect to the construct of the American Depositary Receipts (ADRs)[383], the upvaluation of intermediates will make sense.

Reforms in this area are absolutely necessary to ensure cross-border voting, as the current state of law impedes the economically essential free flow of funds but also hinders effective monitoring of the investments. Appropriate regulation may even build an often-demanded link to exercise a certain control over globalisation.

6.5.4. Conclusion

The future of voting will not have much in common with the practice existing in Germany so far. The retreat of the custodian banks and the arrival of modern communication technologies in the Stock Corporation Act will alter the status of shareholders in Germany considerably. Whether this development will enhance the position of all shareholders is questionable. This derives from the fact that electronic proxy voting is, with the exception of RWE, only made possible for AGMs of companies issuing registered shares (in Germany: about 10% registered shares, 90 % bearer shares) and that proxy voting services are (as yet) contracting only institutional investors. Therefore the majority of small private shareholders will face difficulties when trying to carry out their shareholders' rights. However, it should not be neglected that the new environment will certainly enhance pluralism and responsibility at the shareholder meetings. New communication possibilities will ease the distribution of information to

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382 "Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe" (2002) to download at http://europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf at p.55

383 Definition: see Appendices at Definitions

shareholders and should improve their opinion-forming process. At least the availability of alternative analysis of the agenda will be enhanced.

6.6. Right to File a Suit

The most powerful instrument for the shareholder in the case of a dispute with the stock corporation is the right to file a suit. A number of courses are possible for the shareholder, depending on the infringement by the corporation.

In first place the appeal against a general meeting resolution (Anfechtungsklage - § 246 AktG) should be mentioned.

The second possibility is to take a nullity action (Nichtigkeitsklage - § 249 AktG). In contrast to the appeal action, where ruling in favour of the investor leaves room to reshape the resolution, in this case the court will void the corporate resolution.

It is also possible to file an action for damages (Schadensersatzklage). Unfortunately, shareholders in Germany had to experience the break down of the former Neuer Markt to realise the law did not provide even fundamental shareholder protection. With the introduction of the Anlegerschutzverbesser-ungsgesetz (Act to Protect the Investor), the legislator has addressed this issue. This act converts the EU- Direction on Market Abuse in the areas of capital market information and the protection from undue market practices and extends it to investment forms, which are not vested in securities. Now shareholder protection is enhanced regarding insider trading, ad hoc publication and market manipulation.

The shareholder may also file an appeal according to § 243 s.2 AktG if another shareholder used his voting right to get himself or a third party special advantages, or a procedure to enforce information according to § 132 AktG.

To complete the legal protection of the shareholder, he could also apply a judgement procedure according to the Spruchverfahrensgesetz (Judgement Procedure Act), if he seeks compensation following entrepreneurial restructuring measures of the company.

6.6.1. Checking Resolutions

In general the Stock Corporation Act differentiates between nullity (a grave infringement of the law so no action is necessary) and contestability (a less serious infringement of law and therefore dependent on an appeal, which could make the resolution inoperative) where a stakeholder has filed an action against a resolution of the general meeting.

6.6.1.1. Appeal against General Meeting Resolutions

6.6.1.1.1. Technical Introduction

Any shareholder may file an appeal against a general meeting resolution (§ 245 AktG) if he stated his protest in evidence[384], or has not been invited properly. The same right is granted to management and, under certain circumstances, even to members of the management or supervisory board.

A prerequisite is that the law or the articles of association have been infringed (§ 243 s.1 AktG). In this context, irregularities arising from the resolution are quite important. The prevalent opinion supports the view that irregularities, which have become causal for the coming about of the resolution lead to the annulment of the latter[385]. Usually these shortcomings are results of formal mistakes, unequal treatment of shareholders or infringements of law[386]. Absolutely necessary for the appeal is that the month's grace is met (§ 246 s.1 AktG).

Unsuccessful appeals against resolutions are valid, even if they do not meet the requirements stated in the law or in the articles of association. Surely it must be recognised that this rule is restricted. If the resolution endangers the public interest or the protection of the creditor it is nullified[387].

A requirement regarding the number of shares necessary to file a suit does not exist. Hence, one share with the nominal amount of one Euro is sufficient for an action against a resolution[388].

Baums explains in his working paper "Die Anfechtung von Hauptversammlungsbeschlüssen" that it is not necessary for the plaintiff to claim that he was infringed in his rights as a shareholder. His interest that the resolution should conform to the law and the articles of association is sufficient[389]. This comprehensive legal protection is difficult to understand. Why should a shareholder have the right to take an action when a third shareholder was not invited properly and therefore was not able to vote, or was excluded from the option to subscribe in the case of an increase in

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384 This could only be the case if the shareholder attended the meeting personally. As the represented shareholder is not able to state his protest in evidence he is not entitled to sue (exemption, when the proxy stated the protest in evidence). Among other reasons this explains why most often shareholder associations are the plaintiffs.

385 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.491

386 Some examples cover the areas of: a formal mistake - e.g. formal shortcomings with the notice to the general meeting (no concrete intervention in participation rights); mistakes with the preparation of resolutions and realisation of the meeting - e.g. notice to an inadmissible place - § 121 s.4 AktG (no concrete intervention in participation rights); infringement of participation rights, especially information rights - e.g. § 131 AktG; mistakes with the findings in the resolution - e.g. mistakes with the majority; general infringements of the law; unequal treatment of shareholders; objective contents control and breach of trust - e.g. duty of loyalty; acceptance of special advantages – e.g. a special advantage to a certain circle of shareholders. In-depth with a number of rulings: Hopt, Klaus J./ Wiedemnann, Herbert „Großkommentar zum Aktiengesetz" 4th Edition Berlin 1995 at § 243 from no. 15 (p.62) (Schmidt)

387 § 241 AktG

388 § 8 s.2 AktG

389 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.2

capital stock? It can only be assumed that if there were not the considerable costs of litigation, this right of action would allow a flood of 'white knights' who were only acting on behalf of the shareholders. It is worth discussing whether the shareholder has to maintain his interest for the duration of the suit. However, to avoid abuse this needs to be answered in the affirmative.

The material resolution control is the crucial review criteria. This ruling by the Bundesgerichtshof in "Kali und Salz" [390] should be qualified by saying that this statement is only valid for certain resolutions[391]. Furthermore, since the "Linotype"-case[392] the duty of loyalty, under certain circumstances, is also seen as an object of the resolution control.

6.6.1.1.2. § 243 s.2 s.1 AktG

It is important to mention the justification of an appeal according to § 243 s.2 s.1 AktG. A suit could be based on the reason that a shareholder used his voting rights to achieve special benefits for himself or a third party, and that the resolution has served this purpose. As this norm ignores safeguarding the interests of the creditor, it is restrictively applied in its practical use[393]. Therefore it is only consistent if this provision will be annulled.

6.6.1.1.3. Shareholders' Reasons for the Appeal

An important reason for an appeal is the increase of capital stock. According to § 255 AktG this proceeding is not only possible in the case of an increase in capital stock by contributions but also when the issue or minimum price is too low and the acquisition right of the shareholder has been ruled out. The purpose of this norm is to increase protection for the minority shareholder and in contrast to § 243 s.2 AktG it does not consider subjective elements[394].

255 s.1 and 3 are superfluous and s.2 could be seen as equivalent to § 243 s.2 despite the subjective elements[395]. Therefore it is disappointing that with the reform of the Spruchverfahren (judgement procedure)[396] the legislator missed the opportunity to include this proceeding. On account of the fact that the majority of the appeals have the purpose of finding adequate compensation, this step should have been obvious.

As it can bee seen in figure 26, further reasons for an appeal against a resolution are manifold.

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390 Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs in Zivilsachen - BGHZ Volume 71 at p.40, 43, 49

391 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.4

392 Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs in Zivilsachen - BGHZ Volume 103 at p.184,193

393 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.58

394 Korpff, Bruno/Semler, Johannes „Münchner Kommentar zum Aktiengesetz" Munich 2001 at § 255 No.2 (Hüffer)

395 „Aktiengesetz -Großkommentar" 4th Edition, 6th installment, Berlin New York 1996 at § 255 No.1 (Schmidt)

396 see Chapter 6.2.6.1.4.2. Spruchverfahrensgesetz (Judgement Procedure Act)

Figure 26: Further Reasons for an Appeal against a Resolution (1980-1999)[397]

Contested Resolution	Number of Appeals
Discharge	69 (24%)
Resolutions regarding the utilization of returns	10 (3%)
Elections to supervisory board	18 (6%)
Restructuring	33 (12%)
Statement of annual accounts	6 (2%)
Capital measures	53 (18%)
Election of auditor	13 (5%)
Issue of "Wandelschuldverschreibungen"/optional bonds and bonus shares	9 (3%)
Alteration of articles of association	34 (12%)
Resolutions according to § 119 Abs. 2 AktG	8 (3%)
Winding up respectively liquidation resolutions	4 (1%)
Company contracts	17 (6%)
Other	13 (5%)

Thereby the plaintiffs claim a number of different infringements[398], mostly formal mistakes forming the majority. Taking all this into account it is astonishing that only thirteen actions have been taken, reprimanding the infringement of the articles of association[399].

6.6.1.2. Nullity Action

Closely related to the appeal against the resolution is the nullity action. This form of legal action aims to set aside a resolution. Any shareholder, the management, or a member of the management or the supervisory board is entitled to take a nullity action against a resolution of the general meeting. It is even possible to assert the nullity other than by filing a suit[400]. Reasons for nullity include resolutions endangering the public

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397 Baums, Theodor/ Vogel, Hans-Gert/Tacheva, Maja „Rechtstatsachen zur Beschlusskontrolle im Aktienrecht" 2000 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.86 at p.12

398 E. g.: infringement of regulations regarding the election and composition of the supervisory board; infringement of report and formal requirements according to the law of conversion (91 cases); in the case of discharges, a breach of duty of the management might be claimed (22); often violations of the duty to inform and to report (87); also popular are formal mistakes regarding the preparation and summoning of the general meeting (55) - Baums, Theodor/ Vogel, Hans-Gert/Tacheva, Maja „Rechtstatsachen zur Beschlusskontrolle im Aktienrecht" 2000 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.86 at p.12

399 More detailed regarding the reasons for appeals: Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p. 12ff, Baums, Theodor/ Vogel, Hans-Gert/Tacheva, Maja „Rechtstatsachen zur Beschlusskontrolle im Aktienrecht" 2000 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.86 p.12ff

400 § 249 AktG

interest or the protection of the creditor as stated in § 241 AktG. However, as it is an exceptional norm a number of other reasons could be claimed by the plaintiff[401].
It is essential in this proceeding that the plaintiff is a shareholder during all stages of the suit[402], although it is not necessary that he held shares at the time the resolution was passed. There is debate as to whether a plaintiff (no shareholder) could alter his petition through a declaratory action[403] into an action to nullify, if he becomes a shareholder before the last oral hearing.
Additionally, the Stock Corporation Act provides in § 242 AktG the possibility to cure the nullity. Here it is stated[404] that shortcomings can be cured with entry in the commercial register. Furthermore, the new release procedure according to § 246a AktG should be taken into account.

6.6.1.3. Positive Proceeding to Approve a Resolution

It is also relevant to mention the positive proceeding to approve a resolution. This proceeding becomes relevant when the forming of the resolution is not in question, but the chairman of the AGM used the wrong means of approval and thus made it contestable. Having said that, it needs to be mentioned that this proceeding does not have a major impact on the legal practice.

6.6.1.4. Further Proceedings

6.6.1.4.1. § 243 s.2 AktG - Compensation Contra Appeal

§ 243 s.2 s.2 AktG provides that an appeal according to § 243 s.2 s.1 AktG (a shareholder used his voting rights to achieve special benefits for himself or a third party and the resolution has served this purpose) is possible when appropriate compensation was not offered.
There is plenty of criticism of this provision. Authors like Hüffer[405], Schmidt[406] or Zöller[407] argue that this norm does not meet the creditor protection. Also a case is made of the possibility to buy out the right of appeal against the will of the shareholder. In

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401 E.g.: Grave shortcomings with the notice to the general meeting§ 121 s.2, 3, 4 AktG; formal shortcomings according to § 130 s.1, 2, 4 AktG; incompatibility with the essence of the corporation or infringement of provisions, which protect the creditor or the public interest (limited application possibility – only with shortcomings in the content); violating good morals (limited application possibility); resolution that is in conflict with a resolution regarding the conditional capital increase (§ 192 s.4 AktG); infringement of principle: shareholders are entitled to subscribe new shares equivalent to their interest of the capital stock (§ 212 s.2 AktG); § 217 s.2, § 228 s.2 § 234 s.3, § 235 s.2 AktG become invalid if the decision is recorded on the commercial register in a certain time frame; successful contest against a resolution (see below); final ruling to cross out resolutions in the commercial register officially. Furthermore, specific reasons for nullity are standardised too; election of members of the supervisory board (§ 250 AktG); resolution regarding the utilisation of the balance sheet profit (§ 253 AktG); nullity of the annual balance – only applicable for the general meeting, as generally the board has already passed the annual balance (§ 256 s.3 AktG).

402 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 249 No. 29

403 § 256 ZPO

404 Exception: § 242 s.2 s.4 AktG

405 Hüffer, Uwe „Aktiengesetz" 6th Edition Munich 2004, § 243 No.37 and No.40

406 „Aktiengesetz – Großkommentar" Berlin, New York 1996 4th Edition at § 243 No.59 (Schmidt)

407 Zöllner, Wofgang(Editor) "Kölner Kommentar zum Aktiengesetz" 2nd Edition, Cologne 1988 at § 243 No.236

practice the application of § 243 s.2 s.2 AktG is, because of an infringement of the equal treatment principle[408] and of the duty of loyalty (in detail see Chapter 7) of the majority shareholder, handled restrictively. The compensation must be made from the company's assets[409].
Creditor protection is up to a point ensured by the "German system"; the creditor is also a major investor (Custodian banks/institutional investors control up to 80% of the votes). Having said that, it could even be claimed that the creditor/investor has the freedom of choice between creditor protection by voting against a resolution, or as an investor by filing a suit for compensation.
As Geßler[410] states, the protection of the shareholder is limited to the avoidance of economic loss.
Furthermore, if § 243 s.2 s.2 AktG becomes relevant the investors are at risk of losing their borrowing power. Hence, such a step should always be the result of a well thought-out and balanced process.
In Germany creditor protection compared to shareholder protection is always of major importance.

In the case of a squeeze out the majority shareholder also seeks to achieve a special benefit by paying compensation, even though this might be against the will of the shareholder. The same is valid in a compensation payment following a takeover. Therefore trying to hold up the concept of creditor protection against the just mentioned cases is contradictory and also inconsequent. As already said with respect to the equal treatment principle it could be alleged that an adequate compensation is in the interest of the shareholder and therefore is not inconsistent with § 53a AktG.
A breach of the duty of loyalty is certainly more serious. Here the course of law must be open to the shareholder and hence, § 243 s.2 s.2 AktG is not applicable.

As a conclusion, § 243 s.2 s.2 AktG is too restrictive. A more generous interpretation of the norm would certainly benefit the vast majority of investors who are interested in shareholder value.
It is questionable to use the argument of creditor protection. As has been stated, most creditors also control the vast majority of votes (custodian banks). Logically this would mean that any resolution in a general meeting, which aims at creditor protection (e.g. dividend payments) must be scrutinised carefully as it could simply have the function to benefit those investors who are also creditors. Therefore the argument for creditor protection is counterproductive.

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408 § 53a AktG

409 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.59

410 Geßler, Ernst „Zur Anfechtung wegen Strebens nach Sondervorteilen nach § 243 s.2 AktG" in „Festschrift für Barz" 1974 at p.103

What certainly counts is the duty of loyalty. In this case no restriction should be made as this could encourage major investors to pursue company-destructive policies.

6.6.1.4.2. Spruchverfahrensgesetz (Judgement Procedure Act)

This proceeding allows a legal remedy for minority shareholders who have a right of compensation where the company has carried out entrepreneurial restructuring measures (§ 1 SpruchG). The great advantage of this proceeding is that it is neither necessary to block AGM resolutions[411] nor, with respect to § 246a AktG, to pursue a release procedure.

The judgement procedure was considerably altered by the legislator in 2002 and was transferred to the Judgement Procedure Act. This became necessary due to the introduction of the Corporate Governance Code. Another reason was the length of the judgement procedure that existed up until then. Due to the complexity of the valuation, the claiming shareholder often had to wait years until awarded compensation[412]. In addition to that it is expected that the importance of this proceeding will be enhanced in the ensuing years. Not least because the German Government introduced in a new act (WpÜG - Wertpapiererwerbs- und Übernahmegesetz (Security Acquisition and Takeover Act)) the possibility to squeeze out minority shareholders. Whether this made another act necessary remains to be seen.

Fortunately the legislator has removed a warped condition[413] with this new act. In § 15 s.1 UmwG the legislator explicitly manifested that the shareholder of the takeover company could also file a petition to determine an appropriate extra payment if the exchange ratio was too low.

It is incomprehensible that the judgement procedure is not applicable when a shareholder was excluded from the option to subscribe for shares in the case of an increase in capital stock.

The argument that a fixing of the issue could not be considered due to the enormous organisational expenses, which will arise for the issuing banks or for the issuer itself (whoever will carry the costs)[414] is not convincing. These expenses will also emerge following a successful appeal against the resolution.

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411 Gesetzentwurf der Bundesregierung "Entwurf eines Gesetzes zur Neuordnung des gesellschaftsrechtlichen Spruchverfahrens (Spruchverfahrensneuordnungsgesetz)" 2004 to download at http://dip.bundestag.de/btd/15/003/1500371.pdf at A; The BGH has even ruled that shortcumings in the information flow regarding the valuation should only be denounced in the Spruchverfahren. (Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs in Zivilsachen - BGHZ Volume 146, 179).

412 Gesetzentwurf der Bundesregierung "Entwurf eines Gesetzes zur Neuordnung des gesellschaftsrechtlichen Spruchverfahrens (Spruchverfahrensneuordnungsgesetz)" 2004 to download at http://dip.bundestag.de/btd/15/003/1500371.pdf at I. 1.

413 Bayer, Walter „Kapitalerhöhung mit Bezugsrechtsausschluss und Vermögensschutz der Aktionäre nach § 255 s.2 AktG" in Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht (ZHR) Volume 163 (1999) p.505-553 at p. 547; Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.64

414 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.66

The same is valid for the opinion that the shareholders prefer to appeal against the exclusion itself and not the price for which they are entitled to buy the new stocks[415].
First of all the shareholder will seek compensation for lost profit. Even when he claims to have an interest in an appeal against a resolution it could be assumed that it is driven by the demand to not be financially worse off than other shareholders. If this is not the case, another interest of the minority shareholder could be assessed as an abuse of a right[416]. From a typical point of view the shares of minority shareholders are essentially regarded as capital investment[417]. The stock corporation must have a noteworthy entrepreneurial interest in structural and company-related measures[418].
The issuer can pay the compensation as a cash settlement. If a corporation decides to exclude the option to subscribe it could be expected that this measure is balanced and well thought-out. Hence, an increase in capital stock on one side and the danger of a compensation payment on the other do not exclude each other.
Furthermore, if an increase in capital should be carried out by investments in kind, the judgement procedure is also appropriate, as it presents a property asset and can, therefore, follow a stock price.
This measure by management is for a number of reasons (no encroachment in the property, market pressure, no structural and qualitative dissimilarity between a merger and an increase in capital[419]) not as drastic as in the case of a squeeze out.

To draw a conclusion, a judgement procedure will not only accelerate the proceeding (§ 9 SpruchG) as shareholders could be compensated faster, but will also give all parties more comfortable legal protection (no blocking of resolutions), whilst at the same time maintaining shareholder rights. Promoting this course of law is truly a step in the right direction, as it will at least ease the workload of the courts.

6.6.1.4.3. Squeeze Out and Integration
The concept of a squeeze out describes the buy-up of shares by the majority shareholder in order to obtain 100 percent of them. Although this occurrence has a negative connotation it is most often based on reasonable and necessary economic decisions. For example the realisation of necessary structural reforms is far less complicated and cost intensive when there is only a single shareholder involved as there is no need for a general meeting and therefore no blocking of reforms and no formal requirements with regard to shareholders. The Stock Corporation Act provides in § 327a s.1 s.1 AktG that

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415 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 152

416 Compare with: Hirte, Heribert/Von Bülow, Christoph "Kölner Kommentar zum WpÜG" Cologne 2003 at § 327a AktG No. 11 (Hasselbach)

417 Geibel, Stephan/Süßmann, Rainer „Wertpapiererwerbs- und Übernahmegesetz" Munich 2002 at Art.7 § 327a AktG No.29 (Grzimek)

418 Hirte, Heribert/Von Bülow, Christoph "Kölner Kommentar zum WpÜG" Cologne 2003 at § 327a AktG No. 11 (Hasselbach)

419 Bayer, Walter „Kapitalerhöhung mit Bezugsrechtsausschluss und Vermögensschutz der Aktionäre nach § 255 s.2 AktG" in Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht (ZHR) 163. Volume (1999) p.505-553 at p. 551

the general meeting could decide the transfer of shares by the minority shareholders to the majority shareholder on the condition that he holds 95 percent of shares or more. As a countermove they are granted a reasonable compensation in cash. To strengthen the position of the investor the Bundesverfassungsgericht (Federal Constitutional Court) ruled[420] that the compensation must not ignore an existing market price. Although the minority shareholder is not entitled to file a suit according to § 327f s.1 s.1 AktG in conjunction with § 243 s.2 AktG against this "squeeze out", he has the possibility of nominating a judgement procedure for a legal inspection of the granted compensation - or where compensation is not offered, or incorrectly offered, inspection as to why this was the case[421].

The same course of law is open to excluded shareholders of an integrated company[422]. They are also entitled to obtain compensation, which they cannot claim by means of an appeal against the resolution, but by applying a judgement procedure for legal inspection.

When assessing these provisions, which made their way into the Judgement Procedure Act, it can be assumed that the legislator recognised that shareholding is a form of investment rather than a claim for possession. Hopefully this realisation will also find its way into the reform of the appeal against a resolution, which aims at compensation rather than safeguarding of ownership.

6.6.1.4.4. Procedure to Enforce Information (§ 132 AktG)

The procedure of enforcing information is quite unspectacular, only becoming relevant when the management board refuses to provide information. The shareholder can either take an action according to § 132 AktG to enforce the information that was rejected in the general meeting, or appeal against a resolution according to § 243 s.1 AktG. As both proceedings have different aspirations, they are independent from each other and thus can be pursued in parallel. Although this measure seems to be too expensive for the small private shareholder it might be crucial for the institutional investor, as it could influence his recommendations, and capital market decisions are based on this information.

A precondition to enforce information legally is that the refusal of information is stated in evidence. This may be enforced by the affected shareholder[423].

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420 BVerfG, 1 BvR 1613/94 (27.4.1999) at No.61 to be downloaded at

http://www.bverfg.de/entscheidungen/rs19990427_1bvr161394.html?Suchbegriff=B%F6rsenkurs

421 § 327f s.1 s.2, 3 AktG

422 § 320 AktG

423 § 131 s.5 AktG

6.6.1.5. *New Possibility for the Company: The Release Proceeding (§ 246a AktG)*

With the release proceeding, the UMAG implemented one central demand of the Corporate Governance Commission. Although this new provision primarily serves the interest of the company it also has a considerable impact on the shareholders and their engagement of an appeal or nullity action.

According to § 246a AktG it is possible for the corporation to circumvent the blocking impact of the appeal or nullity action. However, the release proceeding is only open for structure-changing resolutions, which require registration. In other words the corporation could choose this course of law in the case of capital measures, which aim to increase or decrease the capital stock as well as in the case of company contracts. Other registration requiring resolutions, especially further changing of the articles of association, are not subject to this legal remedy.

Hence, according to § 246a s.1 AktG the company could file an application to the process court. The aim will be to achieve a statement that the filed suit does not oppose the registration of the resolution and that faults of the resolution do not affect registration. Consequently, this means that even a successful appeal or nullity action cannot rescind registration[424]. Crucial for the ruling of the court in a release procedure is less the case of an inadmissible suit, but the question if the suit is obviously baseless or if the validity of the resolution is primarily to avert substantial disadvantages from the company or its shareholders[425]. Schütz explains that the suit is seen as obviously baseless, when this could be predicted with a high certainty[426]. The aversion of substantial disadvantages is subjected to careful consideration of all interests by the court[427].

At this point it should be added that § 246a AktG is subsidiary to § 16 s.3 UmwG and § 319 s.6 AktG, which also provide release proceedings.

Hirschberger[428] sees the release procedure quite critical. According to him, the investment of a single shareholder has an economic and rational basis. Therefore it would be more beneficial to protect the single shareholder through Capital Market Law instead through Company Law[429]. Additionally, due to the different periods of time for the appeal, the release procedure and the appeal against the release decision, Hirschberger calculates that a delay of seven months could occur, which would make

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424 § 242 s.2 s.6 AktG in conjunction with § 144 s.2 FGG

425 § 246a s.2 AktG

426 Schütz, Carsten„Neuerungen im Anfechtungsrecht durch den Referentenentwurf des Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" in Der Betrieb (DB) 2004 pp.419-426 at p.424

427 Schütz, Carsten„Neuerungen im Anfechtungsrecht durch den Referentenentwurf des Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" in Der Betrieb (DB) 2004 pp.419-426 at p.424

428 Hirschberger, Max „Das Freigabeverfahren für Hauptversammlungsbeschlüsse nach dem UMAG-Entwurf (§ 246a AktG-E) – Ein Aus für „räuberische" Aktionäre?" in Der Betrieb Number 21 21.05.2004 p.1137-1139

429 Hirschberger, Max „Das Freigabeverfahren für Hauptversammlungsbeschlüsse nach dem UMAG-Entwurf (§ 246a AktG-E) – Ein Aus für „räuberische" Aktionäre?" in Der Betrieb Number 21 21.05.2004 p.1137-1139 at p.1138

the intention of the release procedure superfluous[430]. Even though his opinion is well founded and thus should not be ignored, the release procedure has to be seen as a compromise. It should maintain legal protection to the plaintiff without endangering the economic interest of the company. Although a clear cut with respect to the right of action might have been more beneficial not only for the company but also for all stakeholders, this legal reform will hopefully serve its purpose: to limit the abuse of the right to appeal.

To draw a conclusion, it is simply understandable that in certain cases the request of the company to register the resolution prevails over the interest of the plaintiff to block the resolution, especially as his right to claim compensation remains untouched and hence, is at least subsidiary.

6.6.1.6. Effect of the Ruling

It is important to add at this point that a decision that rules a resolution invalid cannot be registered if a legally binding finding according to § 246a s.1 s.1 AktG is effective.
However, in cases where the release proceeding is not applied and the final ruling has declared the resolution invalid, the resolution will be quashed.
According to § 244 AktG it is possible that the issuer repairs the contestable resolution. With this step the corporation could avoid an appeal precautionary. When the plaintiff has succeeded in a nullity action a healing is not possible.

6.6.1.7. Abuse of the Right to File a Suit

Unfortunately, before the presentation of the UMAG there had been considerable abuse of the right to file a suit. This was also acknowledged by the Bundesgerichtshof[431]. As Baums points out, filing a suit with the intention to achieve a profitable settlement or getting an exaggerated compensation for "legal consulting" has been quite popular with some active shareholders[432]. Quite easily, resolutions could be blocked by a shareholder until he received a financial settlement for the withdrawal of his action. At the same time it has been difficult to find a correlation between the abuse and a specific

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430 Hirschberger, Max „Das Freigabeverfahren für Hauptversammlungsbeschlüsse nach dem UMAG-Entwurf (§ 246a AktG-E) – Ein Aus für „räuberische" Aktionäre?" in Der Betrieb Number 21 21.05.2004 p.1137-1139 at p.1138

431 Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs _ BGHZ Volume 107 at p. 296, 308 ff ; Hüffer, Uwe „Aktiengesetz" 6th Edition Munich 2004 at § 245 No.22

432 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.14, 15; Baums, Theodor shows in this study, among other interesting statistics, that 11 shareholders were responsible for at least 50 % of 408 actions taken against AGM resolutions between the years 1980 and 1998. They are even named and listed according to the number of their appeals in Baums, Theodor/ Vogel, Hans-Gert/Tacheva, Maja „Rechtstatsachen zur Beschlusskontrolle im Aktienrecht" 2000 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.86 at p.10

shareholder right[433]. This fact increased the difficulty of the legislator to take selective action against the abuse. However, due to the increased awareness of stock corporations, who now approach certain issues at an AGM with greater care and the mentioned acknowledgment by the BGH that the right to file a suit could be abused, these kinds of actions have been repelled. Furthermore, with the release proceeding according to § 246a AktG, abusing legal suits will be more difficult as such suits will be dismissed by court more easily.

Of interest is the fact that the vast majority of proceedings (79%[434]) end in a ruling. Only 11 % ended in settlement, which was the desired outcome for a shareholder taking such action.

6.6.2. Reforming the Contestability of Resolutions

In the past, abuse of appeal or nullity actions almost reduced this legal remedy to an absurd move, although the stock corporations and courts targeted a number of procedures displaying signs of abuse[435].

Conditions for the appeal or nullity action led to discussion as to how this system could be reformed so that only legitimate procedures are taken to court. Some suggestions were taken up by the legislator and documented in the new UMAG[436]. Baums, and the Government Panel on Corporate Governance, who developed some of the proposals, supported the idea of the suspension of the blocking effect[437]. A summary review determines whether the appeal (only against alteration of the articles of association, capital measures and approval of company contracts) is likely to be successful and therefore the interest in the suspension of the blocking effect is justified. If this is not the case, a register blockade is not possible when the company has a prevailing interest in the registration. With regard to the possibility to set aside the blockade of the register in the case of mergers, takeovers and other transformations[438] that already existed, the Government Panel on Corporate Governance suggested modifying the phrasing of the proceeding from "obviously baseless" to "adequate chances of success"[439].

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433 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p. 15

434 Figures taken from: Baums, Theodor/ Vogel, Hans-Gert/Tacheva, Maja „Rechtstatsachen zur Beschlusskontrolle im Aktienrecht" 2000 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.86 at p.16

435 Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs _ BGHZ Volume 107, 296, 308 ff; Henze, Hartwig „Höchstrichterliche Rechtsprechung zum Aktienrecht" 3. Aufl. 1997, S. 390 ff.

436 Bundesjustizministerium "Entwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" 2004 to download at http://www.bmj.bund.de/media/archive/701.pdf

437 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.98 ff; Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 153

438 § 319 s.6 AktG, § 16 s.3 UmwG

439 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.109

Another idea implemented in the UMAG was to impose a duty to publish settlements on the webpage, in the papers of the company and the Bundesanzeiger. This suggestion became supportable, not at least because of its salutary preventive function[440].

However, if the new provisions in the UMAG will serve the purpose of opposing the abuse of the right to file a suit has yet to be proved. Consequently, it has to be doubted whether the legislator will consider new measures before the UMAG has shown its effectiveness.
Taking into account that not only the abuse of the right to file an action should be on trial, further points at issue should be considered when scrutinising reform of the system.

Further suggestions in the pipeline to reform the shareholder's right of action beyond the UMAG should include explanation and examination of the following:
It is discussed to introduce a certain quorum of the capital stock to make a shareholder or pool of shareholders become entitled to file a suit[441]. So far even the One-€uro-Share fulfils the right of action. This idea is supported by the argument that a shareholder with a splinter interest is more closely related to a creditor with a promissory note on returns, than to a partner. Additionally, it is difficult to demand reasonable behaviour in the interest of the company[442] from quorums comprised of shareholders with objectives driven by increasing shareholder value. Corporate interests such as socially responsible investment and solidarity with a company (as an employee) are beyond the scope of most private shareholders.
In contrast to these ideas the government panel on corporate governance states that the shareholder must be able to protect himself against an encroachment in his constitutional ownership laws[443]. In any case it will be difficult to determine a fair quorum and it might be alleged the minority investors' only interest is shareholder value.

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440 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 159; Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.114

441 KRIEGER, Gerd „Aktionärsklage zur Kontrolle des Vorstands- und Aufsichtsratshandelns" in Zeitschrift für das gesamte Handels- und Wirtschaftsrecht (ZHR) Volume 163, 1999 p.343-363 at p.361; WIESEN, Heinrich „Der materielle Gesellschafterschutz: Abfindung und Spruchverfahren" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 1990, p. 503-510 at p. 507; Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 139; Hirschberger, Max „Das Freigabeverfahren für Hauptversammlungsbeschlüsse nach dem UMAG-Entwurf (§ 246a AktG-E) - Ein Aus für „räuberische" Aktionäre?" in Der Betrieb Number 21 21.05.2004 p.1137-1139 at p.1139

442 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.51

443 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 139 - However, they see the possibility to demand a quorum when an appeal because of the claimed infringement of the information right is in the pipeline.

Secondly it is suggested that only an association or a common representative should be entitled to sue[444].

A third opinion suggests a certain time of ownership should be required to avoid the situation where shareholders buy shares only after the notice of the AGM has been given[445]. It should be mentioned that the proof of holding would not be the critical factor[446], regardless of whether the company issues registered or bearer shares. With reference to the waiting period and the accompanying danger of loss of legal protection, this suggestion is also seen as a threat to the capital market – shareholders may postpone their investments.

Fourthly, application of the principle of appropriateness should be taken into account[447]. This infers an action which should be scrutinised from the angle of the duty of loyalty. This solution is also a point at issue[448].

Fifthly, it is well worth evaluating the option of limiting the AGM competences. This becomes clear when scrutinising Figure 7 (Appeals against General Meeting Resolutions). It shows the continuous increase in resolution items per general meeting. Unfortunately, trimming these could result in a wider point of attack for shareholders looking for a reason to appeal. Therefore this solution only promises success with parallel reforms of the articles of association and information policy. However, for reasons of efficiency, legal certainty for the issuers and repelling the abuse of the right of action, this approach is certainly supported.

Sixthly, rather than abolishing the resolution in a successful appeal, a strong opinion pleaded for a partial quashing. This would mean that not the whole resolution is invalid but the part in question[449]. In the case of a takeover this approach is already supported by the argument of increased efficiency. At this point it should be mentioned that a sentence by the court, which binds the issuer to mend the resolution in the case of minor shortcomings is not in the pipeline[450].

With the introduction of the UMAG and its release proceeding, this partial quashing is most probably no longer an issue.

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444 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.54

445 KRIEGER, Gerd „Aktionärsklage zur Kontrolle des Vorstands- und Aufsichtsratshandelns" Zeitschrift für das gesamte Handels- und Wirtschaftsrecht (ZHR) Volume 163, 1999 p.343-363 at p.361; Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.54

446 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 146; Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.54, 55

447 Palandt, Otto/Heinrichs, Helmut "Bürgerliches Gesetzbuch" 59th Edition, Munich 2000 at § 242 No. 53

448 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 150

449 HOMMELHOFF, Peter „Zur Kontrolle strukturändernder Gesellschafterbeschlüsse" in Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR) 1990, p. 447-476 at p.457 ff; Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.80f

450 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung – Unternehmenskontrolle – Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 137

Seventhly, the idea to set aside the settlement should, especially after the release procedure, not be considered seriously[451].
Eighthly, it is demanded that the courts should not hesitate to approve damage claims when the shareholder tried to abuse the right of action[452]. Again, this possibility is not seen without scepticism[453].
Ninthly, a reform of the requirement to state the protest in evidence is not supported[454].
Tenthly, a relief in the case of shortcomings during a decision process is seen in the statutory opening for arbitrational procedures (this is especially the case in smaller, cohesive companies)[455].
Finally, even a repeal of this form of action could be considered. As it has already been shown it could easily be possible in a number of cases to refer the shareholder to the course of law of the judgement procedure. A precondition is the acknowledgment of the fact that the primary interest of the shareholder is to receive compensation rather than being awarded with the quashing of a resolution. The smaller the share of the investor, the easier it is to allege a prevalent interest in compensation. This is the case in a squeeze out for example, as already explained above. Here a breach of the constitutional right of property is disclaimed.
However, one point at issue regarding this suggestion is the probable stimulation of the exit rather than the voice.

Taking all this into account, it must be admitted that the UMAG took some of these suggestions off the agenda. However, it has to be doubted that the introduction of the UMAG was the necessary fundamental alteration of the right of action, as it has been discussed at the 63rd German Lawyers Congress[456].

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451 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.85

452 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 - to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.116

453 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 160

454 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 147

455 Report of the Government Panel on Corporate Governance July 2001 "Unternehmensführung - Unternehmenskontrolle - Modernisierung des Aktienrechts" to download at http://dip.bundestag.de/btd/14/075/1407515.pdf at No. 162

456 Die Beschlüsse des 63. deutschen Juristentages Leipzig - E. Abteilung Wirtschaftsrecht (63rd German Lawyers Congress) 2000 to download at www.djt.de/files/djt/63/wirtschaftsrecht.pdf at E) - Wirtschaftsrecht I 1 A.

6.6.3. Manipulation and Wrong Presentation towards the Capital Markets

6.6.3.1. Compensation Claims against the Issuer

In this section I will introduce a number of claims shareholders could file. This will provide a comprehensive idea how he could seek compensation for the infringed right. For the shareholder such a list is important to articulate his claims in a legal proceeding and to highlight the fact that he has indeed suffered damage.

6.6.3.1.1. Compensation Through §§ 37b and 37 c WpHG

In 2002, §§ 37b and 37c WpHG were introduced by the 4. Finanzmarktförderungsgesetz (Act to Promote the Financial Market). Theses paragraphs provide compensation for investors who suffered damage in trading their securities, because of omitted or late publication or false assertion of potential price-relevant facts by the issuer.

6.6.3.1.2. Further Basis for Compensation

§ 79 AktG: A liability for executive organs[457] is given for the issuer if the management, a member of the management or a so-called constitutional appointed representative have made themselves liable for compensation, and the act was committed in the execution of chores, which they are entitled to execute[458].

§ 823 s.2 BGB in conjunction with § 92 s.1 and s.2 AktG: As per this paragraph a claim could be asserted if the management has infringed its duties in the case of loss, debt overload or insolvency. However, § 92 s.1 and s.2 AktG do not fulfil the necessary requirement for § 823 s.2 BGB of being a protective law. This derives from the fact that this norm has the purpose to restore the information and legal capacity of the general meeting and does not grant individual protection to shareholders[459].

§ 823 s.2 BGB in conjunction with § 93 s.2 AktG: (Typical case: insolvency delaying[460]) Nothing else is valid for a claim via this provision. For shareholders there is neither a basis of claim in § 93 s.2 AktG, nor in § 823 s.2 BGB in conjunction with § 93 s.2 AktG. In addition to that they cannot assert the claim of the issuer[461].

§ 823 s.2 BGB in conjunction with criminal law provisions: Untouched is the possibility to claim compensation when for example a criminal law provision (e.g. § 266 StGB -

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457 § 31 BGB

458 Hüffer, Uwe „Aktiengesetz" 6th Edition Munich 2004, § 79 at No.23

459 Hüffer, Uwe „Aktiengesetz" 6th Edition Munich 2004, § 92 at No.15f; other opinion in Zöllner, Wofgang(Editor) "Kölner Kommentar zum Aktiengesetz" 2nd Edition, Cologne 1988 at § 92 No. 24 (Mertens)

460 Schmidt, Karsten „Gesellschaftsrecht" 4th Edition, Cologne, Berlin, Bonn, Munich 2002 at p.817

461 Hüffer, Uwe „Aktiengesetz" 6th Edition Munich 2004, § 93 at No.19

Breach of Trust or § 399 ff AktG – false information/ presentation of the company's circumstances) is infringed.

6.6.3.2. Compensation Claims, which Could also be Filed against Third Parties

6.6.3.2.1. Manipulation of the Quotation and Market Price According to § 20 a WpHG
In general, this section provides legal security to the shareholder in cases in which a domestic quotation or the market price of an asset is influenced[462]. The act prohibits false assertion of facts relevant for the assessment, or the omission of information as well as acts of deception.
The intended manipulation could be committed in a number of ways[463], such as
- Giving orders with gradually higher prices or high volume orders at the end of the day
- Manipulation through buy-outs, repurchases or price care
- Taking control of demand of the basic value or derivatives, so that they can be manipulated.

It is important to mention that § 20a s.2 WpHG provides the possibility for the Supervisory Authority BAFIN as well as for the Federal Ministry of Finance to introduce statutory instruments, which should function as guidelines. This provision is absolutely necessary to differentiate legal measures, which are for example essential to stabilise the share price.

6.6.3.2.2. Compensation Through § 13 WpÜG
In addition, a shareholder could search for compensation via § 13 s.2 WpÜG. This paragraph regulates the financing of the offer to acquire securities. A distinction should be made between takeover of control and the ordinary acquisition of shares. Regarding the latter, the bidder is free in his choice of the quid pro quo. In contrast to this, the requirements for takeover of control are higher. Cash payments, compensation in liquid securities or securities tradable at a stock exchange in the European economic area, are the common methods of financing in this case. The legislator has rejected any further regulation[464].
This claim could be asserted legally. In this case the opposing party is not the bidder but the financial service corporation that produced a letter of confirmation that the bidder is

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462 Lenzen, Ursula „Das neue Recht der Kursmanipulation" 2002 Paper No. 101 at p.6 to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html

463 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Fortentwicklung des Finanzplatzes Deutschland (Viertes Finanzmarktförderungsgesetz)" 2002 to download at http://dip.bundestag.de/btd/14/080/1408017.pdf at p. 89

464 Vogel, Hans-Gert „Finanzierung von Übernahmeangeboten - Testat und Haftung des Wertpapierdienstleistungsunternehmens nach § 13 WpÜG" to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.97, 2002 at p.3

able to provide the funds necessary to fulfil the offer. It is important to mention that it is possible to agree to an exclusion of liability in the internal relationship[465].

6.6.3.2.3. Ad Hoc Announcements § 15 WpHG

During the hausse at the end of the 1990s and the beginning of the year 2000, ad hoc announcements were used excessively by Neuer Markt companies to market themselves. Often the "breaking news" was more of a hoax than anything else. In order to protect investors, the legislator considerably enhanced requirements for ad hoc announcements with the 4. Finanzmarktförderungsgesetz in 2002[466] and lowered the liability threshold for an offence against the norms in § 15 s.1 to 3 WpHG. However, to underline the fact that this norm is not a protective law (and hence, open to claims in conjunction with § 823 s.2 BGB), and serves only to secure the functioning of the capital markets, a claim should only be possible via §§ 37b and 37c WpHG[467]. In addition to that, sanctions provided by the public law are possible if this norm is culpably infringed[468].

6.6.3.2.4. Prospectus Liability according to § 45 BörsG

Reformed in 1998 by the 3. Finanzmarktförderungsgesetz, § 45 BörsG regulates the liability for false or incomplete prospectuses. The term prospectus relates only to presentations necessary to authorise the securities for trading at a stock exchange. Research reports, ad hoc announcements, advertising measures, etc. do not fall under this provision[469].

The party opposing a claim is, therefore, the one who took responsibility of the prospectus or the one who issued the prospectus[470] (§ 45 s.1 s.1 No.1 and 2). It is necessary to mention in this respect that exculpation is possible[471].

Increasing globalisation has lead not only to greater complexity but also to enhanced competition of financial markets[472]. In any case the investors will carefully scrutinise the different requirement. It will be interesting to observe if a "race to the top" will attract more capital in the competing regimes as shareholders will certainly benefit from these improved requirements.

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465 Vogel, Hans-Gert „Finanzierung von Übernahmeangeboten – Testat und Haftung des Wertpapierdienstleistungsunternehmens nach § 13 WpÜG" to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html Paper No.97, 2002 at p.17

466 § 15 s.1 s2 to 4 WpHG

467 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Fortentwicklung des Finanzplatzes Deutschland (Viertes Finanzmarktförderungsgesetz)" 2002 to download at http://dip.bundestag.de/btd/14/080/1408017.pdf; „Regierungsentwurf eines Vierten Finanzmarktförderungsgesetzes" Zeitschrift für Bankpolitik und Bankpraxis (ZBB)- Dokumentation 6/2001 at p.513

468 Assmann, Heinz-Dieter / Schneider, Uwe H. „Wertpapierhandelsgesetz" 2nd Edition Cologne 1999 at § 15 No.165

469 Groß, Wolfgang „Kapitalmarktrecht – Kommentar zum Börsengesetz, zur Börsenzulassungs-Verordnung, zum Verkaufsprospektgesetz und zur Verkaufsprospektverordnung" 2nd Edition Munich 2002 at §§ 45, 46 BörsG No. 10 ff

470 Groß, Wolfgang „Kapitalmarktrecht – Kommentar zum Börsengesetz, zur Börsenzulassungs-Verordnung, zum Verkaufsprospektgesetz und zur Verkaufsprospektverordnung" 2nd Edition Munich 2002 at §§ 45, 46 BörsG No. 20: This could include anybody who had an interest in the Issue. For example: major shareholders, who try to sell their share, parent companies or members of the supervisory board.

471 § 46 s.1 BörsG

472 Groß, Wolfgang „Kapitalmarktrecht – Kommentar zum Börsengesetz, zur Börsenzulassungs-Verordnung, zum Verkaufsprospektgesetz und zur Verkaufsprospektverordnung" 2nd Edition Munich 2002 at §§ 45, 46 BörsG No. 3

It is also important to mention that §§ 45 ff BörsG are special norms in contrast to §§ 71 ff and 57 AktG. Therefore the latter are subsidiary[473]. This derives not at least from the fact that in this case an internal exclusion of the liability is within the law[474].

6.6.3.2.5. Prospectus Liability according to § 13 VerkProspG

Supplementary to § 45 BörsG is § 13 VerkProspG, which regulates the question of liability for sales prospectuses. Regarding the basis of claim, it refers to §§ 45 to 48 BörsG. This indicates that the rules of these norms, with certain exceptions, also apply for § 13 VerkProspG. Here it is important that the exclusion deadline starts with the first public offer. Hence, the order has to be made during this period of time and must be based on the faulty prospectus.

6.6.3.2.6. Further Basis of Claims

Compensation according to § 826 BGB may also be possible. This provision provides a basis for claims, in the case of wilful immoral damage by the responsible group (e.g. management, shareholder, or creditor), who, for example, pushed investors for hopeless rescue payments[475].

6.6.4. Master Action

In November 2005 the KapMuG[476] – Kapitalanleger-Musterverfahrensgesetz (Act for Master Actions by Investors) became effective. In February 2007 the Oberlandesgericht Stuttgart judged in a Master Action against DaimlerChrsler in favour of the defendant[477].

The main reason for the introduction of this act was the (in April 2007 at the Oberlandesgericht Frankfurt still) pending suit against Telekom. About 15.000 plaintiffs filed a suit against the Deutsche Telekom AG and pleaded that the assessment of the real estates of the company in the year 2000 were wrong, which resulted in a wrong Bourse prospectus. Consequently, it was feared that the lawsuit would take several years. A decision by the Bundesverfassungsgericht, which mentioned that a master action would be more suitable, put the legislator under pressure to make a move[478].

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473 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Fortentwicklung des Finanzplatzes Deutschland (Drittes Finanzmarktförderungsgesetz)" 1998 (BT-Drucksache 13/8933) to download at http://dip.bundestag.de/btd/13/089/1308933.asc at p.54, 78

474 Groß, Wolfgang „Kapitalmarktrecht - Kommentar zum Börsengesetz, zur Börsenzulassungs-Verordnung, zum Verkaufsprospektgesetz und zur Verkaufsprospektverordnung" 2nd Edition Munich 2002 at §§ 45, 46 BörsG No. 8ff

475 Schmidt, Karsten „Gesellschaftsrecht" 4th Edition, Cologne, Berlin, Bonn, Munich 2002 at p.900

476„Gesetz über Musterverfahren in kapitalmarktrechtlichen Streitigkeiten (Kapitalanleger-Musterverfahrensgesetz - KapMuG)" 2005 to download at http://www.bafin.de/gesetze/kapmug.htm

477 OLG Stuttgart, 901 Kap 1/06 (15.2.2007)

478 Möllers, Thomas M.J./Weichert, Timan "Das Kapitalanleger-Musterverfahrensgesetz" in Neue Juristische Wochenschrift (NJW), No.38, 2005, p.2737-2741 at p.2737

By bundling capital market-related legal disputes, a master action should be created, which will improve the collective enforcement of shareholder claims. Not only will this new master action ease the workload of the civil courts, but it will also help to avoid complex and similar evidence-taking in a number of proceedings. Additionally, the KapMuG will strengthen the supervisory authority; foster legal security as diverging decisions will be avoided, and most importantly will improve the enforcement possibilities of the individual investor through proportionate distribution of costs. The KapMuG's range of application concerns faulty information, which for instance includes incorrect prospectus or incorrect ad-hoc announcements, at the capital market[479].

It is essential to point out that a bundling only takes place with regard to the master action. Consequently, it is still necessary that every shareholder needs to file his claim individually[480]. Aim of the master action is to come to a decision in advance over single facts of the case, conditions or legal questions[481].

The application for a master action could be made by the plaintiff or the defendant. To do so, the applicant needs to state that the findings of a master action will have implications for other similar lawsuits[482]. In order to make other shareholders who have been harmed aware of the master action, it will be published in the Bundesanzeiger[483]. Important to add is that the court of competent jurisdiction will name a master plaintiff according to its own consideration. Thereby the court will consider the significance of the plaintiff's claim and the acceptance of the other plaintiffs[484]. This procedure was introduced to avoid a "race to the courtroom" as it frequently happens in connection with security class actions in the U.S.[485]. The decision in the master action develops a commitment effect.

Attention should be drawn to Article 9 KapMuG, which states that the act is effective for five years. This indicates that it was introduced in order to collect experiences first before turning it into a permanent act. The introduction of the KapMuG should improve the protection of the shareholder. Whether it is a successful tool remains to be seen.

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479 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Einführung von Kapitalanleger-Musterverfahren" 2004 to download at http://www.bmj.de/media/archive/798.pdf at p.1

480 Möllers, Thomas M.J./Weichert, Timan "Das Kapitalanleger-Musterverfahrensgesetz" in Neue Juristische Wochenschrift (NJW), No.38, 2005, p.2737-2741 at p.2738

481 Reuschle, Fabian "Das Kapitalanleger-Musterverfahrensgesetz" in Neue Zeitschrift für Gesellschaftsrecht (NZG), No.13, 2004, p.590-593 at p.591

482 § 1 s.2 s.3 KapMuG

483 § 2 s.1 KapMuG

484 Möllers, Thomas M.J./Weichert, Timan "Das Kapitalanleger-Musterverfahrensgesetz" in Neue Juristische Wochenschrift (NJW), No.38, 2005, p.2737-2741 at p.2739

485 Reuschle, Fabian "Das Kapitalanleger-Musterverfahrensgesetz" in Neue Zeitschrift für Gesellschaftsrecht (NZG), No.13, 2004, p.590-593 at p.592

Having explained the new German master action, attention should be drawn to the possibility of shareholders joining a class or similar action abroad. Unfortunately, German institutional investors have an aversion against these options. Although the institutional investors are entitled to it, they are reluctant to recover losses on behalf of their clients. Certainly economical factors will make filing a claim unattractive in some cases. However, in the US compensation payments became enormous[486]. Although there is no legal obligation to join a Security Class Action it is the fiduciary responsibility of Kapitalanlagegesellschaften to maximise the contributions to their clients. Consequently, the latter should insist that a respective clause is stated in the contracts.

6.6.5. Investors via Kapitalanlagegesellschaften

Fund investors are also protected with the ability to claim for damages where a causal and culpable infringement of administrative care and due diligence by the fund management has occurred[487].
Such cases may be as straightforward as culpable infringement of a contract of agency[488]. More complex situations can arise where fund management has infringed an individual protecting statute according to § 823 s.2 BGB[489].

Damages claims may also be based on prospect liability[490], provided that the investor has bought shares based on incorrect specifications in a prospect or brochure. The legislator has tightened this direction to damage claims by demanding that the wrongful specifications had to be essential for the valuation of the shares. Nevertheless, it should be questioned whether the statement that the fund manager will fulfil his "fiduciary duties" or "is responsible" is essential for valuation. Although these concepts are certainly phrased very gently, they are of importance from the angle of corporate governance, but from the angle of valuation, the importance is questionable. An investor who buys units in a fund certainly gets a positive impression through the fulfilment of fiduciary duties[491]. Additionally, investment in a responsible fund is more probable than investment in a fund that abstains from its fiduciary responsibilities. However, should a fund promoting the compliance of fiduciary duties to increase its market share while knowing that it never intends to address its national/international voting rights, be targeted by prospect liability? Again the question of the appraisability

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486 Settlements in the Pipeline in October 2005: >13 Billion US$ - Source: Institutional Shareholder Services

487 Brinkhaus, Josef/Scherer, Peter „Gesetz über Kapitalanlagegesellschaften – Auslandinvestment-Gesetz", Munich 2003 at § 10 I No.26 (Schödermeier/Baltzer)

488 §§ 675, 611 in conjunction with §§ 280 ff BGB

489 For example § 278 BGB (agent who is subjected to directions), §§ 276, 31 BGB (infringement of contract) or § 831 BGB (agent).

490 § 127 s.1 s.1 InvG

491 Brinkhaus, Josef/Scherer, Peter „Gesetz über Kapitalanlagegesellschaften – Auslandinvestment-Gesetz", Munich 2003 at § 20 II No.7 (Schödermeier/Baltzer)

(Bewertbarkeit) of voting rights arises and, unfortunately, it is doubtful whether courts will acknowledge this appraisability.

The pursuit of fiduciary responsibilities incurs costs[492] that are passed on to the investor. Investors in such firms demonstrate that they are willing to pay extra for a responsibly managed fund. Valuation of his investment is also determined by this factor, with the result that responsible investment is essential. To what extent courts will follow such an argument remains open. The reasoning will probably follow arguments of economic reason[493].

Finally, the claims have to be asserted, either by the custodian bank on behalf of the shareholders, or by the shareholders themselves.

6.6.6. Legal Costs

The cost of litigation must also be considered. Where a stock corporation is defeated in an appeal against a resolution or in a nullity action, it is according to § 91 ZPO (Zivilprozessordnung – Civil Process Rule) and § 247 AktG, obliged to cover the plaintiff's expenses. This payment only extends to reimbursing the investor's cost to initiate the proceeding against the firm, while additional costs, such as those for legal advice, investigations, and time involved to prepare the case, are not covered[494].

However, if the plaintiff does not succeed he has to carry the costs of the litigation. In contrast, the management will pass on the costs to the company in the case of a defeat.

The grand total that may be claimed by the applicants following a ruling in their favour is a decisive factor for an investor to initiate a judgement procedure[495]. This is because, in contrast to the appeal against a resolution or the nullity action, the legal costs have to be covered by the opposing party. This should ensure that a procedure is possible for any shareholder. However, liability of the appealing shareholder is possible on the grounds of equitable principles (abuse of law).

For the sake of completeness it should be mentioned that costs for a private shareholder filing a lawsuit, which could be ascribed to capital market law[496], may be covered by appropriate insurance.

Having explained the legal basis for shareholder engagement, the following chapter will provide a comprehensive insight and discuss the issue of selling the shares. In contrast to the forms of engagement mentioned so far, I will argue that this activity does

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492 E.g. Physical representation by a German Custodian in an AGM on behalf of an institutional investor: 100 €/hour.

493 E.g. Brinkhaus, Josef/Scherer, Peter „Gesetz über Kapitalanlagegesellschaften – Auslandinvestment-Gesetz", Munich 2003 at § 10 II No.10 (Schödermeier/Baltzer)

494 Baums, Theodor „Die Anfechtung von Hauptversammlungsbeschlüssen" Working Paper No. 85, 2000 – to download at http://www.jura.uni-frankfurt.de/ifawz1/baums/Arbeitspapiere.html at p.32

495 § 15 SpruchG

496 BGH IV ZR 327/02

not really agree with the idea of corporate governance. Selling the shares, or "exit" can only be treated as a last resort when all forms of engagement have failed.

6.7. Selling the Shares and Shareholder Engagement

Selling the shares has also been referred to as "voting with the feet", or as "exit" in contrast to the use of shareholder "voice". In this respect Arnswald, in citing Hirschman, points out that "exit belongs to the realm of economics, voice belongs to the realm of politics"[497].

Although Figure 17 indicates that institutional investors increasingly use the voting right and contact the company directly to communicate issues, the selling of the shares remains a popular tool to avoid negative consequences.

The shareholder could actively control the corporation, but he also has the option of expressing his discontentment with management by selling his shares, and in the case of struggling companies, may avoid heavy losses by doing so. Not only is this an easy course of action, but it also has a side effect. Through selling the shares pressure is put on management to increase the company's performance. Indeed, this "side effect" is arguably all the more significant precisely in markets where long term or relational shareholding is practised. In such countries, for instance Continental Europe (in contrast to Anglo-American regimes) selling the shares could be seen as active governance because the ending of a long-term relationship puts a higher strain on the board. According to Hirschman "... it is very likely that the very process of decline activates certain counterforces"[498]. Whether this statement corresponds to the facts will be discussed in detail below.

While some authors see the possibility of exiting the business as contradicting the exercise of governance[499], other writers deny to mention this option[500]. However, both groups view the determining factor as the liquidity of the secondary market (stock exchange), although they see different conditions for their conclusions. Therefore a closer look is necessary.

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497 Arnswald, Ulrich "Hirschman's Theory of Exit, Voice, and Loyalty Reconsidered", European Institute for International Affairs Heidelberg 1997 at p.11

498 Hirschman, Albert „Exit, Voice and Loyalty: Responses to Decline in Firms, Organisations and States " Harvard University Press, Cambridge 1970 at p. 15

499 All authors take liquidity thoughts as a basis - Coffee, John „Liquidity versus Control: The Institutional Investor as Monitor" in Columbia Law Review, Vol. 91 No. 6, 1991 p.1277-1368; Bolton, Patrik/von Thadden, Ernst-Ludwig "Blocks, Liquidity and Corporate Control" in the Journal of Finance, Vol.53, No.1, 1998 at p.1-25; Bhide, Amar "The Hidden Costs of Stock Market Liquidity" in Journal of Financial Economics, Vol.89, 1993 at p.31-51; Admati, Anat/Pfleiderer, Paul/Zechner, Josef "Large Shareholder Activism, Risk Sharing and Financial Market Equilibrium" in Journal of Political Economy, Vol.102, No.6 1994 at p.1097-1130

500 All authors assume the existence of asymmetric distribution of information (characteristic of the Principal-Agent-Theory) - Holström, Bengt/Tirole, Jean „Market Liquidity and Performance Monitoring" in Journal of Political Economy, Vol.101, No.4, 1993 at p.249-259; Kahn, Charles/Winton, Andrew „Ownership Structure, Speculation and Shareholder Intervention" in Journal of Finance, Vol.53, No.1, 1998 at p.99-129; Maug, Ernst „Large Shareholders as Monitors: Is there a Trade-Off between Liquidity and Control?" in Journal of Finance, Vol.53, No.1, 1998, at p.65-98

6.7.1. Denying the Correlation between Selling the Shares and Corporate Governance

Representatives of this opinion do not deny that selling shares is a form of corporate governance, but from their point of view selling the shares does not correlate with corporate governance. For them the driving force of active governance is the performance of the stock market.

Deriving from the hypothesis that an asymmetric distribution of information will lower the equity prices at the secondary market, Steiger expresses the opinion that this bear market will lead to enhanced control of the corporation[501]. The grade of information undoubtedly influences the behaviour of the investor[502], while the source of the information, whether it is of public or inside origin[503], does not matter. Followers of this opinion argue that the possibility of higher rates at the secondary market will increase efforts of institutional investors to sell shares, as the expected gains will more than compensate for the governance costs. Hence, the Free Rider Problem does not exist within these theories[504].

For a number of good reasons, however, it seems that the metaphor does not work. These include the facts that the capital presence in general meetings is very low, even though the custodian banks already provide a considerable number of votes; that institutional investors are not interested in blocking shares; and that there is divergence between the activism of pension funds and investment funds.

The assumptions of this hypothesis are certainly not baseless, especially as the exit (depending on the size of the investor) could place considerable strain on the secondary market, which cannot be in anybody's interest. However, the weakness of the theory mentioned above could be the insufficient differentiation of the groups of investors (Hedge funds which aim on a short term profit maximisation on the one side and long term orientated pension funds on the other side) and the missing time frame for the observations.

6.7.2. Selling the Shares as an Alternative to Corporate Governance

Providing that the secondary market for the issued share is endowed with sufficient liquidity, selling appears a desirable option, as it is easy to buy and sell without fear of a negative market impact[505]. However, the question remains if it is an alternative to corporate governance. As mentioned above, a number of authors answer this in the

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501 Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance" Baden-Baden 2000 at p.104

502 Erlei,Matthias/Schmidt-Mohr, Udo in "Gabler Wirtschaftslexikon" 15th Edition Wiesbaden 2000 at p.2481

503 Eatwell, John/Milgate, Murray/Newman, Peter "The New Palgrave - A Dictionary of Economics" London and Basingstoke 1987 at Volume 3 p.677-679 "trading on information in financial markets"

504 Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance" Baden-Baden 2000 at p.138

505 Strenger, Christian „Corporate Governance - The Viewpoint of a Large Institutional Investor" in Schwalbach, Joachim „Corporate Governance - Essays in Honor of Horst Albach" Berlin, Heidelberg 2001p.163-172 at p.169

affirmative. Not only do they come to this conclusion because of the passivity of a large number of institutional investors (with the exception of some pension funds like CalPERS, TIAA-CREF or Hermes) but also because of the dispersal of their shares. This feature suggests that a trade-off between liquidity and governance exists. Depending on the investment policy the interest an institutional investor usually holds in a company could be relatively small. This generates a readiness to sell the shares in a short time frame, although this can have negative effects on the stock price.
Primary investment in shares to provide a moderate amount of liquidity (compared to the size of the fund) and the readiness to hold them over a short time, underline the assumption that institutional investors prefer to sell rather than become involved in corporate policy. An additional reason might also be the governance costs, which are considerable, while the effect of corporate governance on the stock price is positive, but not determinable.

However, the studies on this issue mentioned above do not differentiate between the groups of shareholders. Like the empirical investigations[506] these research papers only confirm the investment policy of the institutional investors instead of analysing if exit is a desirable tool to pursue corporate governance and hence their significance is limited.
This theory is also disproved by increased involvement of institutional investors in corporate governance, even though it might only be used as a promotional tool. Additionally, selling the shares provides no guarantee that the new owner of the shares will take measures to correct the original problem. This means from the perspective of a market regulator and the economy as a whole that use of exit as an exclusive remedy could increase the number of avoidable corporate failures and reduce market efficiency[507]. Such a result is not desirable.

Having explained that selling the shares is no alternative to corporate governance, it could be deduced that it might serve as an additional tool in the concept of corporate governance.

6.7.3. Is Exit a Completion of Corporate Governance?

An association can be drawn between shareholder engagement as an active form of corporate governance, and selling shares as a passive form. This assumes shareholder engagement is only practised when effort and costs come at least close to the declared target, whether this is monetary or social. Therefore if this is not the case, a reasonable investor would sell his shares, rather than engaging with management.

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506 Steiger, Max „Institutionelle Investoren im Spannungsfeld zwischen Aktienmarktliquidität und Corporate Governance" Baden-Baden 2000 at p.218-261

507 Donald, C. David "Shareholder Voice and its Oponents" Institute for Law and Finance – Johann Wofgang Goethe Universität; Working Paper Series No.40; 06/2005 at p.3

Hence, when the profit on the stock price is higher than the governance costs the investor would become active, if not he would prefer to sell. Since the profit achieved by active corporate governance is rarely determinable, either the governance costs for the investor have to be very small (as is certainly the case in a free rider situation), or the expected profit has to be considerable for governance policies to be worthwhile. Given this, will the trade off influence the behaviour of the management?

Providing the liquidity of shares is limited, exit of a group of investors will increase pressure on the remaining shareholders rather than raising pressure on management, although the danger of a takeover is also increased. The management could even become counterproductive by presenting the company in a better light than it really is (Enron, Worldcom and Parmalat are good examples of this) to avoid the exit of investors. As Driver and Thompson point out, the management is more likely to promote a healthy business instead of introducing unpopular measures, which will adversely affect the employees[508] or themselves. Therefore the danger is that stabilising the share price is a more important item on the agenda than introducing measures to emphasise necessary reforms.

Taking these points of view into account the consequence must be that selling the shares is not the completion of corporate governance. Too many bad examples in corporate history have shown that, in certain cases, it is counterproductive and could even have negative effects on the economy.

6.7.4. Increased Influence of Active Shareholders

When a group of shareholders decides to sell their shares, the remaining investors are under more pressure to take an active role in governing the company and force management to increase its efforts. If they are not prepared to make losses by trading off their shares, they are left with the choices of either waiting until the crisis has passed, or seeking means to be corporately active. To opt for the latter has advantages for the stakeholder. Such advantages are that their share is enhanced because of the increased selling activity; other shareholders are now more prepared to support the trailblazer; and the influence and power of the board is diminished. Taking this into account the position of the remaining shareholders is increased. Hence, becoming active

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508 Driver, Ciaran /Thompson, Grahame "Corporate Governance and Democracy: The Stakeholder Debate Revisited" 2001 to download at http://www.open.ac.uk/socialsciences/staff/gthompson/Corporate%20Governance%20and%20Democracy.pdf - The authors provide a number of arguments, which favour the role of stakeholders rather than shareholders. They conclude that in creating systems of countervailing power, it is necessary to move beyond the level of the corporation. Hence, confining stake holding to the firm involves a bias against broader interests - including customers, suppliers, the environment and even those not working or small entrepreneurs. However, their study does not cover the case of a struggling company, where the shareholders has the choice between exit or voice.

is an attractive possibility for them. To give an example, in 2002 the Deutsche Telekom share price dropped to less than ten per cent of its highest fixture, while the remuneration of the board members rose by 90% in one year. Incumbent CEO Ron Sommer started a campaign to show that the company's situation was far better than the share price reflected. This was not successful and the supervisory board forced him to step down. This followed by a demand from the federal government, as the major investor with a share of 43%, to change corporate policy and the composition of the board.

Increased influence is part of the reason why some fund managers (e.g. Hermes) explicitly search for weak stock, which they then buy cheaply. Installing governance-related structure helps to regain the firm's lost ground before they sell their shares, often with considerable gain.

6.7.5. Conclusion

The option of selling the shares is Janus-faced with regard to the impact on corporate governance. On one side a management under pressure is likely to protect its own stakes and present the company to be more attractive than it actually is, on the other side remaining shareholders become more influential, and get more active. Having highlighted this inconsistency, it needs to be concluded that selling shares does not support corporate governance. Although the exit could have positive side effects such as the increased opportunity for shareholder engagement, the risk of negative effects is also present.

In any case shares are sold to avoid or minimise risks. Therefore the statement that selling shares equals "voting with the feet" is misleading. It is not related to the forms of shareholder engagement mentioned already. The "exit" can only be seen as a last resort when all other forms of engagement have failed.

6.8. Completion of Shareholder Rights: Asset Protection and Dividend Claim

Although asset protection and dividend claim do not belong to the hierarchy of shareholder engagement, they are also shareholder rights. Along with the request for information, speaking at the general meeting, the use of the voting right and the possibility to take legal action this claim completes the list of shareholder rights. Therefore in order to provide a comprehensive view of shareholder engagement and rights, asset protection and dividend claim should be explained briefly at this point.

Probably the most important property right is the claim of a dividend, if the corporation has settled a declaration of dividends in accordance with §§ 60 s.1, 58 s.4, 174 AktG[509]. In contrast to the habit of US-American companies, in Germany the dividend is paid only once a year[510], but the dividend does not necessarily need to be paid monetarily. It could also be a payment in kind if it is stated in the articles of association. A humorous example of such a payment was the case of the Walder Bräu AG (former Brauerei Hänle) in Königseggwald. In 2003 this brewery paid its shareholders a dividend of five boxes of beer.

Often ignored with respect to dividend payments is the issue of withholding tax. On dividends paid by issuers listed abroad, tax is normally charged by the respective national government. However, no distinction is made between national and foreign investors - both shareholder types pay the same tax. Although the paid tax could be claimed back when double taxation occurs, investors usually do not make very much use of this right[511]. It should be emphasised that this should be a fiduciary responsibility of any institutional investor providing that the cost justifies the expected returns.

Necessary to mention is also § 271 s.1 AktG. According to this regulation the shareholder has the right to claim the distribution of any assets of the bankrupted company, which remain after the fulfilment of all liabilities. The leading opinion, stated in the comments of Hüffer and Hoffmann-Becking, endorses a restrictive clause in the articles of association[512]. This is certainly right. However, the norm has the purpose of protecting the assets of the investor.

The shareholder is also entitled to claim an allocation of new shares according to his interest in the capital stock (i.e. he has a "right of pre-emption")[513]. If possible, the type of shares corresponds to the stakeholders' present shares. Only the person who presents the dividend coupon (also termed pledged proprietor) is entitled to the new stocks[514].

Finally, with regard to shareholder engagement it is important to mention that the shareholder is also entitled to dispose of the shares in his ownership as he wishes (e.g. sale, donation, transfer of ownership by way of security, pledge). Therefore the voting right is generally attached to the share - an issue, which frequently comes up with share

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509 Eisenhardt, Ulrich "Gesellschaftsrecht" 10th Edition Munich 2002 at No.622

510 § 174 s1 s.1 AktG

511 According to Goal (www.goalgroup.com) six Billion US-Dollars of withholding tax remains unclaimed each year.

512 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 271 no 2 and Hoffmann-Becking, Michael "Münchner Handbuch des Gesellschaftsrecht - Band 4 Aktiengesellschaft" 2nd Edition Munich 1999 § 66 No.16 (Hoffmann-Becking)

513 § 186 s.1 s.1 AktG

514 Hüffer, Uwe "Aktiengesetz" 6th Edition Munich 2004 at § 186 No. 13 and Hoffmann-Becking, Michael "Münchner Handbuch des Gesellschaftsrecht - Band 4 Aktiengesellschaft" 2nd Edition Munich 1999 § 56 No. 57ff (Krieger)

lending. To give an example, in the case of a usufruct the usufructuary is entitled to vote (§ 22 s.1 No.4 WpHG). The International Corporate Governance Network (ICGN) addressed this concern and formulated a Code of Best Practise[515] also to improve the use of the voting right.

Chapter 6 provided the hierarchy of shareholder engagement according to Company Law by giving an in-depth idea of the rights which the investor could pursue. As proved, the engagement could be quite comprehensive. Therefore it is important to point out that shareholder engagement has its limits, and the investor must take this into account when performing his activity. The following Chapter will explain the limit imposed by the duty of loyalty in detail.

515 International Corporate Governance Network "ICGN Stock Lending Code of Best Practice" 2005, to download at http://www.icgn.org/organisation/documents/slc/code_final.pdf

7. Chapter: The Shareholders' Duty of Loyalty

With respect to the hierarchy of shareholder engagement the duty of loyalty applies to the usage of the voting right. Although it also serves to limit the right to file an action, courts have not sanctioned shareholders yet when they did not comply with this rule. The other forms of engagement are not limited by the duty of loyalty. However, in general Hirschman acknowledges that "…. the likelihood of voice increases with the degree of loyalty"[516]. Consequently, in reverse it is possible to say that the duty of loyalty enhances shareholder engagement.

In Germany the right of disposal, including the exercise of shareholder rights, is limited by Article 14 s.2 s.1 Grundgesetz. Here it is stated that property comes with obligations. Consequently, the existence of the duty of loyalty is not only legally accepted in German law but also has a constitutional basis. As it is also almost undisputed in modern publications, this construct provides the legal limits of share ownership and consequently, the exercise of shareholder rights according to the claimed hierarchy.

The Duty of Loyalty obliges the investor to exercise his membership rights, especially his co-administration and control rights, with respect to the corporate interest of the other investors[517]. Therefore, the scope of this duty is wider than the prohibition of illegal behaviour. In the individual case it could impose duties on the shareholder to set aside his individual interests in favour of those of the corporation or other shareholders[518].

The basics for the limitation of the membership and engagement rights derive from §§ 242 and 705 BGB - elements of confidence protection and the obligation to promote shareholding on the one side, and legal restriction on the other[519]. The consequence of a violation of this norm could be compensation payments according to § 826 BGB.

To simplify matters, the duty of loyalty can be divided into four categories[520]:

1. Duties of conduct in the market (e.g. insider trading (§ 38 WpHG), and offers for take-overs.
2. Asset protection of shareholders (e.g. hidden dividend payouts, excessive compensations in subsidiary companies).
3. Loyal behaviour in conjunction with voting (e.g. blocking essential resolutions, evasion of voting restrictions).

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516 Hirschman, Albert„Exit, Voice and Loyalty: Responses to Decline in Firms, Organisations and States " Harvard University Press, Cambridge 1970 at p.77

517 Schmidt, Karsten „Gesellschaftsrecht" 4th Edition Cologne, Berlin, Bonn, Munich 2002 at p. 592

518 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.183

519 Obermüller, Werner, Winden „Die Hauptversammlung der Aktiengesellschaft" revised by Butzke, Volker 4th Edition Stuttgart 2001 at p.183

520 Timm, Wolfram „Treuepflichten im Aktienrecht" in Wertpapiermitteilungen 1991 p.481-494 at p.483

4. Loyal behaviour in conjunction with the right of action (e.g. abuse of the appeal against general meeting resolutions)

Having named these, it should be emphasised that the consequence of infringements varies. Points one and two, which are less relevant for shareholder engagement, oblige the offender to pay compensation. Disloyal behaviour in conjunction with voting makes the resolution contestable or the offender receives a fine. Finally, the abuse of the right of action does not provide a sanction at all.

Almost unanimous consensus exists in the literature when it comes to the duty of loyalty for the majority shareholder with respect to the minority being protected. There is, however, disagreement whether the duty of loyalty exists between minority shareholders inter-se[521]. While some authors[522] promote an effect-related duty of loyalty, others object this approach. They claim that a shareholder ignoring the necessary consideration of company concerns and the interests of fellow shareholders breaches a duty of loyalty. This latter opinion has to be preferred as Bungeroth[523] explains adequately: It is not a matter of loyalty but one of causality as to whether the investor's behaviour results in damage (e.g. accidental majority) or not. This means that the latter opinion pledges for a stronger assessment of the cause (negligence, gross negligence or intent) instead of the damage.

In practice, the behaviour of large shareholders is naturally subject to higher standards and scrutinised more carefully than the behaviour of small investors. Nevertheless, crucial for an offence against the duty of loyalty is not only the extent of the interest infringement but also if the shareholder acts as an entrepreneur or a simple investor[524], and the size of the company. It could also be assumed that greater standards for share ownership and engagement apply to smaller, non-listed corporations as the number of investors is usually kept within manageable limits compared to public companies.

At this point it should be remembered that the nature and extent of the duty of loyalty is relatively unclear. This is undesirable, given the importance of transparency and clarity in Company Law. In order to avoid abuse and excessive application of the duty of loyalty it is therefore essential that the limits are clearly pointed out[525].

In the "Linotype" decision by the Federal High Court[526] the jurisdiction stated for the first time the limits of shareholder engagement by acknowledging a duty of loyalty by the investor, not only towards the company but also towards other shareholders.

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521 Nodoushani, Andreas „Die Treuepflicht der Aktionäre und ihrer Stimmrechtsvertreter" Baden-Baden 1997 from p.51ff

522 Wolfgang Zöllner in „Kölner Kommentar zum Aktiengesetz" Einleitungsband 1st Edition No.169

523 Kropff, Bruno/Semler, Johannes „Münchner Kommentar zum Aktiengesetz" Volume 2 §§ 53a-75, 2nd Edition Munich 2003 at Vor § 53a No.21 (Bungeroth)

524 Schmidt, Karsten „Gesellschaftsrecht" 4th Edition Cologne, Berlin, Bonn, Munich 2002 at p. 592

525 Kropff, Bruno/Semler, Johannes „Münchner Kommentar zum Aktiengesetz" Volume 2 §§ 53a-75, 2nd Edition Munich 2003 at Vor § 53a No.25 (Bungeroth)

526 Federal High Court - Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs - BGHZ Volume 103 at p.184

In this case the majority shareholder, who had held 96% of the shares and thus the votes, decided to liquidate the company in order to buy essential parts of it cheaply in the progress of the winding up. Due to already existing arrangements between the management and the majority shareholder it was not possible for the minority shareholder to acquire parts of the company. The BGH did not see an infringement of the duty of loyalty in the liquidation decision itself, but saw it in the accompanying circumstances.

Until this decision was made, it was seen as neither necessary nor justifiable to define a comprehensive corporate legal duty of loyalty reaching beyond the general legal principles of §§ 226, 242, 826 BGB. This assumption was additionally justified by the law. This derives from the fact that the shareholder is mostly independent. Additionally, the by-laws[527] sometimes can only be amended under strict rules and conditions (e.g. § 26 s.5 AktG states that fixings regarding the capital structure can only be altered 30 years after the company was registered and when the legal relationships, on which the fixings are based, have been wound up for at least five years). Moreover, the organisational structure of the company (Management board, supervisory board, general meeting) and numerous protective rules existing in Company Law also serve to avoid the abuse of power[528].

It has been shown that in Germany the introduction of a duty of loyalty, especially in the light of shareholder engagement, is essential for corporate Germany and does not contradict the right of free property disposal.

This is in contrast to what is accepted in the United Kingdom for example. Although there are exceptional legal areas where the law accepts some limit on the shareholder's freedom to vote as she pleases. In general shareholders are not subject to any duties towards their fellow shareholders or the management. It is argued that shares are the personal property of the shareholder. For example in *North-West Transportation v Beatty* it was ruled: "In general, the right of a shareholder to vote is regarded as a right of property, which he is entitled to cast in his own interests"[529]. He is not bound to cast his vote in the company's interests[530]. However, the court will intervene if, for instance, a resolution to alter the articles deprives the minority shareholders of their share of the company's assets[531]. Therefore the tests (laid down in *Allen v Gold Reefs of West Africa Ltd* and *Greenhalgh v Arderne Cinemas Ltd*)[532] are that the resolution must be passed bona fide for the benefit of the company as a whole. The effect of the resolution must not be

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527 § 26 s.5 AktG

528 §§ 117, 243 s.2, §§ 300 ff, 309, 311 ff AktG - Kropff, Bruno/Semler, Johannes „Münchner Kommentar zum Aktiengesetz" Volume 2 §§ 53a-75, 2nd Edition Munich 2003 at Vor § 53a No.17 (Bungeroth)

529 North-West Transportation Co Ltd v Beatty (1887) 12 App Cas 589 (PC), at p.593

530 The Law Commission "Shareholder Remedies" (1996) at p. 20 to download at www.lawcom.gov.uk/files/cp142.pdf

531 Buckley, On the Companies Acts (1981) 14 th Edition Vol 1 p.971

532 Allen v. Gold Reefs of West Africa Ltd. [1900] 1 Ch. 656; Greenhalgh v Arderne Cinemas Ltd [1951] Ch 286

to discriminate between the majority and minority shareholders. The former should not get an advantage of which the latter is deprived[533].
Attention should also be drawn to clause 216 of the Company Reform Bill[534]. This section proposes that in future, ratification of a director's breach of duty will be effective only if pursued by members without "personal interest" in the ratification.

Although the legislation in the UK explicitly acknowledges the right of shareholder property, it imposes some limits to the disposal of such property, which at least indicates the existence of fundamental principles of the duty of loyalty.

Having mentioned UK law above, the existence of a duty of loyalty is also known in US law (e.g. Illinois: *Hagshenas v. Gaylord* (1990)[535]) and in certain circumstances even imposed on minority shareholders[536]. Moreover, the duties and responsibilities of corporate directors and controlling persons (including shareholders) were already comprehensive[537] and have even been increased by the Sarbanes-Oxley Act (2002).
Donald[538] explains that under Delaware Law, and the laws of most U.S. jurisdictions, currently a shareholder owes a fiduciary duty to the corporation and any minority shareholder if he either owns a majority in, or exercises control over, the business affairs of the corporation[539]. He adds that this rule is also imposed on minority shareholders if it can be verified that they dominate and control corporate conduct[540].

An exemplary conflict between the duty of loyalty and the right of free property disposal could be seen in the pursuit of an investment philosophy like SRI. In the case of the latter, Rounds points out that

> "Social investing is a precarious investment philosophy that cannot help but reflect the personal, financial, social, and/or political predilections of the investor. Human nature being what it is, trustees will always be tempted to practice social investing in derogation of their fiduciary duty of undivided loyalty."

533 Greenhalgh v Arderne Cinemas Ltd [1951] Ch 286, 291

534 Clause 216, Company Law Reform Bill to download at http://www.publications.parliament.uk/pa/ld200506/ldbills/034/06034.97-103.html#ratif

535 Hagshenas v. Gaylord, 557 N.E.2d 316, 323 (Ill. App. 1990), appeal denied, 561 N.E.2d 691 (1990)

536 United States Court of Appeals for the Seventh Circuit; No. 94-2529, REXFORD RAND CORPORATION v. GREGORY ANCEL, Appeal from the United States District Court for the Northern District of Illinois, Eastern Division. No. 93 C 7386 (1995)

537 Listed and Explained in GIL, Andres V. "Legal Duties and Responsibilities of Corporate Directors and Controlling Persons of U.S. Publicly-Owned Companies", 1995, to download at http://www.natlaw.com/pubs/usmxlaw/usmjnm1.htm

538 Donald, C. David "Shareholder Voice and its Oponents" Institute for Law and Finance – Johann Wofgang Goethe Universität; Working Paper Series No.40; 06/2005

539 Donald, C. David "Shareholder Voice and its Oponents" Institute for Law and Finance – Johann Wofgang Goethe Universität; Working Paper Series No.40; 06/2005 at p.16

540 Citon v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 70 (Del. 1989)

> He further argues that "such nonfinancial considerations necessarily divide fiduciaries' loyalty to the financial interests of their beneficiaries. The financial performance of SRI is "legally irrelevant" as the loyalty line has already been crossed"[541].

Although this opinion raises a critical issue, it does not question the duty of loyalty itself. Instead, it emphasises its importance as an essential basis for the stakeholders.

For the sake of completeness it needs to be mentioned that in Germany, the duty of loyalty is not only imposed on shareholders but also on the company with respect to their shareholders. The company has the duty of enabling every shareholder to pursue his shareholder rights appropriately and without hindrance. Additionally, it has to refrain from any measure which could encroach on these rights[542]. This must be in the interest of the company anyway, as an infringement might pave the way for an action.

Drawing a conclusion, it makes sense that the duty of loyalty applies to the voting right. The right to file a suit is regulated by existing laws and other forms of shareholder engagement do not provide a sufficiently deep possibility to encroach corporate affairs. In contrast to that he voting right in the hands of a majority shareholder could provide a powerful tool, which has to be executed in the interest of all shareholders, while protecting the minority.

The points mentioned above also clarify that the duty of loyalty does not support the possibility of forming alliances or sustain common approaches to issues like class actions, negotiations or overcoming the free-rider problem. At this point in time the duty of loyalty is only imposed on majority shareholders and only when there is a case of a severe infringement of loyalty towards fellow investors. Therefore shareholders who do not fall into this category have the right to dispose freely on their investment. This means that the duty of loyalty cannot impose a positive duty to vote, to participate in an action or in negotiations. Equally, the free-rider problem cannot be solved by the duty of loyalty - agency costs of active shareholders cannot be balanced this way (an alternative solution to this latter issue will be provided later in this thesis (Chapter 10.2.).

Part B described the realisation of shareholder engagement in corporate Germany. It examined how the hierarchy of shareholder engagement could be employed.

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541 Baue, William "Fiduciary Duty, Undivided Loyalty, and Socially Responsible Investment Performance", 2004 to download at http://www.socialfunds.com/news/article.cgi/article1530.html; ROUNDS, Charles "Public Pension Funds, Charitable Funds, and the Social Security Trust Fund: When the State Gets into the Investment Business, Social Investing is Inevitable and there is Little the Law Can Do about it", 2004 at p.1 to download at www.aei.org/docLib/20040604_Rounds.pdf

542 Kropff, Bruno/Semler, Johannes „Münchner Kommentar zum Aktiengesetz" Volume 2 §§ 53a-75, 2nd Edition Munich 2003 at Vor § 53a No.24 (Bungeroth)

Part C will now explain reforms introduced by the legislator as well as theories (including own theories) on further improvement of the shareholder engagement regime in Germany.

Part C - Reform

8. Chapter: A more Detailed Analysis of Recent Legislative Reforms

With a number of initiatives in recent years, the legislator has shown a remarkable activity to reform the Company Law not only in order to keep pace with other financial markets but also to improve the environment for shareholder engagement. Important laws in this area include the Finanzmarktförderungsgesetze (especially the 3rd in 1998 and the 4th in 2002), the KonTraG of 1998, the NaStraG of 2001, the TransPuG of 2002 and the UMAG of 2005 as well as other acts, which only touched on the Company Law in less significant areas. Unfortunately, these acts represent more a "reform in permanence", as Noack[543] describes it and not a fundamental modification of the Company Law. The legislator often does not pass crucial amendments, because the lobby of issuers, Kapitalanlagegesellschaften or custodians oppose these amendments successfully.

Although there are still a lot of legal deficits which have not been removed yet, it can be stated that the German capital market slowly shows the necessary development and strengthens the position of the shareholder.

8.1. The KontraG - Gesetz zur Kontrolle und Transparenz im Unternehmensbereich 1998 (Corporation Control and Transparency Act)

On the 1st of May 1998, the German Government introduced a first wave of reforms towards a more competitive Stock Corporation Act. The new KonTraG can be seen as a first step towards a number of changes made by the legislative body. Other important changes with an impact on corporate governance were made in the "Unternehmens- und Kapitalmarktrecht" (company- and capital market law), the "Gesetz für kleine Aktiengesellschaften" (Act Governing Small Non-listed Stock Corporations) and the "Gesetz zur Deregulierung des Aktienrechts" (Act to Deregulate the Company Law).

The KonTraG[544] primarily focused on the legal requirements of the supervisory board, enhancement of transparency and strengthening of the shareholder meeting.

It provides for management boards of stock corporations being obliged to concern themselves with adequate risk-management and internal revision. Moreover, the duty to inform the supervisory board about future company policy is strengthened.

The number of mandates a member of the supervisory board could have were reduced to ten (by the Corporate Governance Code to five and now the recommendation is

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543 Noack, Ulrich „Neuerungen im Recht der Hauptversammlung durch das Transparenz- und Publizitätsgesetz und den Deutschen Corporate Governance Kodex" in Der Betrieb (DB) 12th Issue 2002 p.620-626 at p.626

544 Shearman, John "Germany – Controlling Directors the German Way" in the Company Lawyer Vol.18 No.4 (1997) p. 123-125 at p.123

scrutinised to reduce it to three!), while the chairman's mandate counts double, and the mandates have to be published. Additionally, annual meetings have to be held at least four times a year. Furthermore, the commission of the final auditor is no longer carried out by the management board, but by the supervisory board. Therefore it is only a logical consequence that it is the duty of the final auditor to be present at the balance meeting of the shareholder representatives' board. He has to present his report to all members of the board. All in all this should provide a greater distance between the auditors and the management. In its report to the general meeting, the supervisory board has to declare how often it has met and how many panels it has formed. Moreover, it has become easier to call the members of the management board or the supervisory board to account for serious misconduct.

In the KonTraG, reforms concerning the shareholder rights have also been introduced. Shareholders now have better access to information concerning the financial situation of the company. Additionally, the practice of proxy voting by banks is more closely related to the interest of the shareholders. Moreover, banks must no longer exercise proxy votes when they own more than 5% of the firm's equity themselves, unless they receive specific voting instructions. However, the practical consequences of the latter will be marginal, since this requirement primarily changes the layout of the forms used to solicit proxy votes[545].

Worth mentioning is also that multiple votes (Mehrstimmrechte)[546] are not possible anymore. The highest voting right (Höchststimmrecht) is only possible in unlisted companies. The cumulating of influence resulting from share ownership and proxy votes of the custodian banks is weakened as § 128 s.2 s.2 AktG now states that the bank has to follow the interest of the represented shareholder and not its own.

To draw a conclusion of the KonTraG, with this Act in 1998 the German Government has started to take care of necessary reforms. Whether these reforms provide a better control over company policy remains unclear. However, the fact that the legislation has recognised the necessity to improve the two-tier system shows that the problems and scandals in the mid-nineties have not been taken as a matter of fact.

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545 Boehmer, Ekkehart "Transparency of Ownership and Control in Germany" 1998 at http://www.wiwi.hu-berlin.de/~boehmer/papers/germany2.pdf at p.23

546 See Chapter 6.2.5.1. Voting Restrictions

8.2. The NaStraG - Gesetz zur Namensaktie und zur Erleichterung der Stimmrechtsausübung 2001 (Law on Registered Shares and Simplified Rules for the Exercise of Voting Rights)

Of course, the wave of new reforms in German Company Law could easily be attached to the demands of an increasingly global economy. However, not only has the legislator become active but also a number of renowned issuers. In order to become more attractive they changed their bearer-share equity into registered shares.

These changes on the German capital market also required consideration by the legislator. Therefore on the 25th of January 2001 the legislator introduced the "Gesetz zur Namensaktie und zur Erleichterung der Stimmrechtsausübung" - Law on Registered Shares and Simplified Rules for the Exercise of Voting Rights (NaStraG) [547]. The intention of accepting new communication forms through the legislator was to allow for the fact that the number of shares and shareholders have increased and have became more global. Although these changes were substantial for the Stock Corporation Act, the formal requirements and the technical proceedings were not reformed[548]. In contrast to the KonTraG, the NaStraG primarily focused on improving the good practice of German companies and therefore did not concentrate on changing the legal environment but instead on improving the possibilities for stock corporations, giving them more organisational independence.

The reforms of the NaStraG have a considerable impact on Company Law as it enables listed German companies to:

-Simplify the exchange of anonymous bearer-share equity into registered shares

-Establish electronic proxy voting to general meetings

-Establish electronic notices of general meetings

-Establish electronic tabulation of vote counts at shareholders' meetings

In addition to that, it includes some alterations in the area of the post formation law (Nachgründungsrecht) and announcements in the commercial register.

The changes of this act met with unanimous approval among the renowned German stock corporations, as it was seen as a tool to encounter the ongoing decrease of capital presence at general meetings in Germany. Maybe there was even hope that NaStraG created the possibility of a higher turn-out at meetings. Unfortunately, the development

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547 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz - NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf

548 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Namensaktiengesetz - NaStraG)" (BT-Drucksache 14/4051) 2000 to download at http://dip.bundestag.de/btd/14/040/1404051.pdf

was slower than expected. Although the capital presence started improving as a result of this reform, it was not yet able to cushion the retreat of the custodian banks.

8.3. The TransPuG - Transparenz- und Publizitätsgesetz 2002 (Transparency and Publicity Act)

First of all, the TransPuG introduced deregulations in the areas of finance, general meeting and information of the shareholders, as well as other thematic focal points like the supervisory board and its supply with information[549]. The TransPuG primarily aimed at broadening the rights of shareholders by introducing good-practice-provisions for German stock corporations. Legally binding reforms were less of the target of this act.
With regard to shareholder engagement, a number of considerable suggestions towards the revaluation of the general meeting, the use of new media, access and quality of corporate information and the jurisdiction were made.

The TransPuG primarily implemented the findings of the Commission "Corporate Governance – Corporate Conduct – Corporate Control – Modernisation of the Stock Corporation Act" and the subsequent Cromme Commission, which created the standards of the German Corporate Governance Code into Company Law.
To point out the significance of the panel's work in formulating the Corporate Governance Code, nearly 150 recommendations for amendments or changes to existing provisions of German law were made. Furthermore, the panel evaluated all proposals on how the German corporate governance system should be further developed in order to maintain a normative framework that is suitable and attractive not only for companies but also for domestic and foreign investors[550].
In the foreword of the German Corporate Governance Code it is stated that[551]: the drawn up Code presents essential statutory regulations for the management and supervision (governance) of German listed companies and contains internationally and nationally recognised standards for good and responsible governance. The Code aims at making the German corporate governance system transparent and understandable. Its purpose is to promote the trust of international and national investors, customers,

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549 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes zur weiteren Reform des Aktien- und Bilanzrechts, zu Transparenz und Publizität (Transparenz- und Publizitätsgesetz)" 2002 to download at http://www.bmj.bund.de/media/archive/301.pdf at p.17

550 Report of the Panel on Corporate Governance to download on http://www.ovs.de/corporate_governance.htm (English conclusion available) or press report 304/01

551 German Corporate Governance Code to download at www.corporate-governance-code.de/eng/download/DCG_K_E200305.pdf at 1. Foreword

employees and the general public in the management and supervision of listed German stock corporations.
The Code was established in § 161 AktG and rules that listed German stock corporations have to explain annually whether they comply with the provisions of the German Corporate Governance Code or not. If they chose not to comply, the corporations have to justify their refusal in the Bundesanzeiger.

With regard to shareholder engagement only those recommendations having an effect on it should be highlighted.
First of all, the introduction of the Bundesanzeiger in an electronic format needs to be pointed out. In contrast to the printed form, the new electronic Bundesanzeiger can provide far more information to the shareholder. In future it is even a possibility to create an uninterrupted information chain to the securities account held online[552].
It is also recommended that the announcement of a general meeting is published on the stock corporation's webpage (Clause 3.2.1 Deutscher Corporate Governance - Kodex). Noack points out that an obligatory publication of general meeting resolutions on the webpage is threatened by nullity action (§ 241 S.1 AktG) while in contrast to that a voluntary publication has no consequences[553].
Furthermore, the German Corporate Governance Code enhanced the duty of the issuer to inform their investors. Now the stock corporation should also send the notice of the general meeting to all domestic and foreign financial services, shareholders and shareholder associations. In general this is also provided by law (§ 125 s.1, s.2 no.1, s.2 no.3, s.5 AktG).
According to the code, additional information such as the annual report should also be provided on the webpage (Clause 2.3.1 Deutscher Corporate Governance - Kodex).
The reform of §126 s.1 AktG certainly aims in the right direction. According to this paragraph, the stock corporation only needs to make counter-proposals to items on the agenda accessible. This means that publishing them on the webpage is legally sufficient. However, this is attached to less of a legal but more of a technical problem. When making counter-proposals accessible on its webpage, the company faces the problem that they become public knowledge. In order to prevent this from occurring, an access code needs to be introduced. Another idea is to inform only the known proxies, associations and custodians about counter-proposals and to make interested shareholders aware of the fact that they could have a look at those when contacting these institutions. For an active investor this is certainly cumbersome but reasonable.

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552 Noack, Ulrich „Neuerungen im Recht der Hauptversammlung durch das Transparenz- und Publizitätsgesetz und den Deutschen Corporate Governance Kodex" in Der Betrieb (DB) 12th Issue 2002 p.620-626 at p.620

553 Noack, Ulrich „Neuerungen im Recht der Hauptversammlung durch das Transparenz- und Publizitätsgesetz und den Deutschen Corporate Governance Kodex" in Der Betrieb (DB) 12th Issue 2002 p.620-626 at p.621

Alternatively, the issuer could also ask the author of the counter-proposal if he objects to a publication of his motion. This matter does occur with issuers of registered shares. However, an improvement regarding shareholder rights is also given by the fact that the time for counter-proposals is extended to one week before the day of the general meeting (so far it has been only one week in total).

A relief for members of the supervisory board is provided in § 118 s.2 AktG. As per this paragraph they could participate via image and sound (e.g. Video screen).
It is also encouraging that the company can include the broadcast of the general meeting in image and sound (§ 118 s.3 AktG) in their articles of association.
Kapitalanlagegesellschaften are now enabled to pass on their votes durably to a proxy. This is certainly a relief as it makes the voting process considerably easier.
Unfortunately, the legislator did not follow the first draft of the bill where the introduction of a record date was planned. With a delay, this provision was taken up by the UMAG and should, therefore, be mentioned again below.
Moreover, the possibility for the shareholder to vote directly online without the requirement of physical presence or the involvement of a proxy was neglected.

To draw a conclusion, the TransPuG is more of a mini-reform than a real improvement of the Stock Corporation Act. Courageous amendments were omitted. Only the most necessary reforms to keep up the pace with other financial markets were realised and a good opportunity was lost. Hopefully the legislator will be more progressive in future reforms.

8.4. The UMAG – Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts 2005 (Act for Enterprise Integrity and the Modernisation of the Right to Appeal)[554]

The latest legal activity, which will take effect probably in the second half of 2005, targets primarily three areas: reform of the right to appeal, the revision of the directors and officers (D&O) liability and the law of the special audit, and the preparation and realisation of AGMs. In this context the UMAG is, because of the legal requirements, comparable to the KonTraG. The essential rules are binding and do not rely on the good practice of the market participants.

Seibert/Schütz[555] emphasises accurately that the UMAG strengthens the conditions of the right to appeal. It enhances the possibility to block important resolutions with a

554Bundesjustizministerium "Entwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)" 2004 to download at http://www.bmj.bund.de/media/archive/701.pdf

single share, while the liability of the corporation has been improved in favour of the shareholder. Here the improvement of the law is significant as financial requirements for shareholders to file a suit have been reduced to 1% of the capital stock or the market value of the shares exceeding 100,000 Euro. This means that now almost any institutional shareholder and a considerable number of private shareholders will be entitled to file a suit.

With respect to the admission of a suit, the enhancement for a second or third filing is remarkable. The course of law in these cases will only be open if the plaintiff provides new information, which is not subject of the first suit. However, with regard to shareholder rights it has to be pointed out that in cases where the rules mentioned above are applied, the company has the right claim and not the shareholder.

A small revolution are the changes provided in § 123 ss.2-4 AktG. Here the legislator recognised the changing shareholder environment towards an increase of global holdings and an enhanced demand for electronic communication, and therefore introduced a record date. This means that the requirement of depositing the shares prior to a general meeting became obsolete. Now the relevant factor is the registration to the general meeting. In the case of bearer shares a certificate by the custodian bank is necessary.

The potential of this reform are expressed by Noack[556]:

> "It is expected that this regulation makes voting for foreign institutional shareholders easier, and that it will fit into the future efforts by the EU with respect to cross border voting."

With the introduction of § 127a AktG, the legislator improves shareholder communication in order to give them the opportunity to organise themselves whenever the law requires value or quorum thresholds. The Bundesanzeiger will provide a "Shareholder Forum" where an investor can file his request, for which he needs a certain stock value or quorum.

In addition to that, the rights of the chairman in the general meeting have been extended (§ 131 s.3, s.6 AktG). With the intention of increasing the efficiency of the shareholder assembly, it is now possible to limit the time for shareholders to hold their speech or ask their questions. Moreover, the company can offer to accept written questions, which it will answer during the meeting. Although this provision guarantees the company flexibility[557], the danger is that floodgates potentially producing contrary effects will be opened, as it is naturally easier to formulate a question in a written form than posing it in front of some hundred shareholders.

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555 Seibert, Ulrich/Schütz, Carsten„Der Referentenentwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts - UMAG" in Zeitschrift für Wirtschaftsrecht (ZIP) 2004 p. 252-258 at p.252

556 Noack, Ulrich „Erleichterung grenzüberschreitender Stimmrechtsausübung - Bericht über eine Initiative der niederländischen Regierung und der Euroäischen Union" in Zeitschrift für Wirtschaftsrecht (ZIP) 2002 p.1215-1216 at p.1215

557 Seibert, Ulrich/Schütz, Carsten „Der Referentenentwurf eines Gesetzes zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts - UMAG" in Zeitschrift für Wirtschaftsrecht (ZIP) 2004 p.252-258 at p.256

Finally, the UMAG also modernised the right to appeal in the new § 243 s.4 s.1 AktG by following the ruling of the BGH[558] (Federal High Court). This paragraph demands that it is now decisive, if a shareholder judging objectively made his actions dependent on the content of the inquiry. Additionally, § 243 s.4 s.2 AktG limited the possibility of an appeal against a resolution when the information duty has been violated.
The introduction of a release procedure for certain structure-changing resolutions (§ 246a AktG for the appeal against a resolution and § 249 s.1 s.1 AktG in connection with § 246a AktG for the nullity action) has also to be assessed as a positive reform. This measure disarms shareholders who simply want to block a resolution with the aim of a lucrative settlement, and enables the corporation to move forward with necessary resolutions, which are in its interest. In other words, although a nullity action or an appeal against the resolution has been successful, the registered resolution cannot be declared invalid by the judgement of the court. However, § 246a s.8 AktG provides compensation for the successfully appealing shareholder.

With regard to shareholder engagement, the UMAG provides a number of positive reforms, which will certainly enhance the ability of investors to become active. In addition to that, the necessary respect and understanding is drawn to the further development of corporate governance.
Nevertheless, it has been critically stated above and should be mentioned here again, that the UMAG is another indicator that the legislator prefers a Company Law reform "in permanence".

8.5. Further Anticipated Legal Reforms

Shareholders could expect a number of legal initiatives in future. This does not only derive from the legal activity of the Securities and Exchange Commission in the last two years and the impact of new regulations by the European Union, but also from the increased importance of the capital market for the pension scheme.

Currently, the legislator plans to scrutinise the liability for false capital market announcements. This initiative is primarily the consequence of the abuse of ad hoc news and other information during the soaring of the Neuer Markt. Unfortunately, the introduction of this act has been postponed until the European Union has clarified its approach to this issue.

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558 Amtliche Sammlung der Entscheidungen des Bundesgerichtshofs - BGHZ Volume 122, p.211

Quite important is the European Commission's Action Plan on modernising Company Law and enhancing corporate governance in the EU[559]. The Commission found that the necessary framework should be developed in a Directive since an effectively exercising these rights requires a number of legal difficulties yet to be solved[560]. This already indicates that the impact of this Directive will be considerable.

Also on a European level, the implementation of the regulations of the Societas Europea into national law could be expected. However, the conversion into respective acts will mostly only affect corporations with European cross-border holdings[561].

Finally, the work of the OECD's Financial Action Task Force on Money Laundering also needs to be mentioned. To avoid the criminal activities of money laundering and financing of terrorist activities, it is being contemplated to abandon the bearer share, or at least to develop this system so that the beneficial owner is made visible.

8.6. Conclusion

There is certainly some truth in the statement that whatever the SEC decides today will become law in Germany five years later. Nevertheless, the German legislator does not only show considerable activity in the regulation or deregulation of the financial market in Germany, but also a sensitive approach in improving the environment for shareholder engagement in order to make it a stronger governor of the company.

This has to be embraced, not only against the background of the corporate scandals but also because of the increasing impact of globalisation on the domestic financial markets and the growing importance of the stock markets for the old-age insurance.

Future legal initiatives will certainly be driven by impacts of the international financial markets instead of national requirements.

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559 European Commission - Directorate General Internal Market „Fostering an Appropriate Regime for Shareholders'Rights" 2004 to download at http://europa.eu.int/comm/internal_market/company/shareholders/ consultation_en.pdf

560 European Commission - Directorate General Internal Market „Fostering an Appropriate Regime for Shareholders'Rights" 2004 to download at http://europa.eu.int/comm/internal_market/company/shareholders/ consultation_en.pdf at p.5

561 Heidel, Thomas "Aktienrecht - Aktiengesetz, Gesellschaftsrecht, Kapitalmarktrecht, Steuerrecht, Europarecht" Bonn 2003 at p.2712

9. Chapter: Theories on the Reform of the System

There are a number of theories on reform of the shareholder engagement system. Some just aim at marginal alterations in the appropriate acts. Others question the system as a whole. Unfortunately, some of these theories are not well thought through, inappropriate for the German legal system, or legal development (e.g. the NaStraG or the TransPuG) has made them superfluous.

With respect to shareholder engagement in Germany, the majority of proposals for reforms aim at the role of custodian banks. Although the criticism of some authors of the current German system is often logical and understandable, they lack a global dimension in a world of Enrons, Worldcoms and Parmalats. Moreover, the introduction of proxy agents provided by stock corporations through § 134 s.3 s.3 AktG forced some custodian banks to pull out of the proxy voting business. Additionally, the losses they produced annually in this area, the bad reputation of this business, and the concentration on the original scopes of business probably made it considerably easy for them to accept it, and even to accelerate this development. Hence, institutional investors will have to conduct their voting independently from the custodian banks in future. This statement is emphasised by the introduction of § 32 s.1 s.4 InvG, which provides that a Kapitalanlagegesellschaft is authorised to appoint somebody to function as a proxy agent only for isolated cases. This means that it is impossible to pass on permanent power of attorney and full discretionary power – a single instruction for each point on the agenda is required. In contrast to the simple representative, an independent proxy voting service could be authorised durably and without instructions (§ 32 I S.5 InvG).

Having emphasised the actual role of the custodian banks in Germany, fundamental theories that go beyond this issue rarely exist (or have already been discussed in this thesis) and thus should not be taken into account in this connection. In the following some theories on the reform of the system are provided. Thereby it needs to be pointed out that although some reforms were developed for an anglo-american legel system they are, at least to a certain extent, also applipicable in Germany.

9.1. Geldmacher

A modern system of proxy voting is promoted by Geldmacher[562]. The intention of his concept is to intensify the contest for the power of disposition on enterprise-tied resources through a separate "trade of votes"[563]. Hence, he favours a market-controlled

562 Geldmacher, Detlef "Marktorientierte Managerkontrolle: Stimmrechte als Kontrollinstrument" 1st Edition, Wiesbaden 2000

563 Geldmacher, Detlef "Marktorientierte Managerkontrolle: Stimmrechte als Kontrollinstrument" 1st Edition, Wiesbaden 2000 at p.248

coordination of proxy votes. He bases his theory on the relationship between vote and share price. The shareholder should be enabled to trade his vote according to a self-determined price. The acquirer will obtain the power of disposition and executes the vote on his behalf, which should have a positive effect on shareholder value.
Undoubtedly, the advantage of this concept is that the cast votes will be used most efficiently. The collector will try to achieve the necessary majority of votes. Thus the danger of accidental majorities no longer exists.
Furthermore, the market of votes could serve as an indicator as to whether a suffering share price is the result of a weakening economy or bad management[564]. Hence, management will be put under pressure when a gap appears between the two rates.
A number of hedge funds already make use of this tool[565]. Black and Hu explain that

> "certain equity derivatives and other capital market developments now allow shareholders to readily decouple voting rights from economic ownership of shares. This decoupling (the new vote buying) is largely undisclosed and unregulated"[566].

Regrettably, Geldmacher's theory and the new capital market developments provide a number of weaknesses and dangers:
Through the introduction of a market for votes, the free-rider problem would be aggravated rather than defused. Firstly, an acquirer would have to carry the governing costs, like those for research or consulting. Secondly, he would be faced with the expenses to gather and cast the necessary votes. Thirdly, the spending for administration should not be underestimated (e.g. contacting the custodians, creating the ballots, etc.).
Furthermore, this opinion does not sufficiently consider the problem that the market for votes would probably become the focus of the shareholders' attention instead of governance issues. Large investors could try to initiate a proxy contest, which they would probably win; not because they have the better arguments, but because they are willing to spend more than the opponent. A good example for this point is a takeover battle.
Finally, a market for votes could infringe the existing law[567]. In § 405 s.3 No.2 and No.3 AktG it is stated that somebody acts against the regulations when he uses somebody else's shares, which he received by granting or the promise of special advantages in a general meeting.
Although this theory provides an interesting approach, it does not provide satisfactory arguments for the discussion of reforming the system.

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564 Geldmacher, Detlef "Marktorientierte Managerkontrolle: Stimmrechte als Kontrollinstrument" 1st Edition, Wiesbaden 2000 at p.279

565 Black, Bernard/Hu, Henry, "Hedge Funds, Insiders, and Empty Voting: Decoupling of Economic and Voting Ownership in Public Companies" March 2006, ECGI - Law Working Paper No. 56/2006, to download at http://ssrn.com/abstract=874098

566 Black, Bernard/Hu, Henry, "Hedge Funds, Insiders, and Empty Voting: Decoupling of Economic and Voting Ownership in Public Companies" March 2006, ECGI - Law Working Paper No. 56/2006, to download at http://ssrn.com/abstract=874098 at Abstract

567 Fraune, Christian "Der Einfluss institutioneller Anleger in der Hauptversammlung" Cologne, Berlin, Bonn, Munich 1996 at p.47

9.2. Latham

An interesting theory was developed by Mark Latham[568]. He suggested the implementation of a "Corporate Monitoring Firm", which does not require a particular board or legal system and hence, is restricted by national circumstances.

According to his view, the shareholders should vote and choose an independent agency for nominating director candidates. This will make directors responsive to owners rather than to management, while avoiding the free-rider[569] problem that limits the effectiveness of other solutions. Furthermore, he suggests that the nominating entity will need to monitor director performance in order to decide whether to select a given candidate again, for the board of the same or another firm. Also it could perform further monitoring functions if requested by a majority of shareholders[570].

Latham highlights that such a "Corporate Monitoring Firm" has the advantage over the system that is existing so far that the intermediate would be paid by each corporation about which they give advise, in accordance with shareholder votes so as to preclude management influence[571]. This payment system is analogous to a citywide tax[572]. In other words, the benefit of this system is undoubtedly the coverage of governance costs by the stock corporations. Through this equilibrium, investors will be afforded an effective pursuit of corporate governance issues.

Latham then continues with a prevailing argument. According to Latham, most important is that the "Corporate Monitoring Firm" would be independent. This would allow the shareholder to make powerful monitoring decisions as several monitoring companies will strive to build a reputation for sound business judgement and independence from the managers of the corporation they monitor. Compared to an individual director, such a firm would provide services to many more client companies over many more years, permitting a far more accurate assessment of its capability[573]. Thus, the alignment of the monitoring firm with the investors will promote more effective governance. In addition to that, directors are chosen by their competence instead of their influence of the electing body. Hence the influence of shareholders will increase, as they can dismiss the monitors annually, and the monitors can dismiss the board[574].

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568 Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm

569 The Free Rider Problem occurs when one investor gets active and carries the costs for his engagement, while shareholders who prefer to stay passive get the benefits of the activity without carrying any expanses.

570 Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm at -2. Solution: A Monitoring Intermediary-

571 Latham, Mark "The Road to Shareowner Power" May 1999 at www.corpmon.com/Road.htm at -Abstract-

572 Latham, Mark "The Road to Shareowner Power" May 1999 at www.corpmon.com/Road.htm at -2. The Free-Rider Problem and Its Solution-

573 Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm at -2. Solution: A Monitoring Intermediary-

574 Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm at -3. Potential Benefits of Monitoring Intermediaries-

A third point favouring this system is the up-valuation of information. In order to provide the shareholders with accurate information, the monitor should go beyond publicly available information, to the point where they would be legally considered insiders. Investors must avoid this possibility or risk having to restrict their trading activity[575].

Finally, he argues that

> "effective shareholder representation at the bargaining table will bring the compensation of top executives closer to the market value of each manager's contribution to the value of the company. Oversight of the process of training and promoting middle managers can prevent a clique from monopolising the knowledge of how to best run the firm[576]."

An assessment of Latham's suggestions is not easy. On the one hand they are well thought through and provide a number of interesting improvements to the proxy system; on the other hand it is questionable whether there is a possibility that this theory could ever become a part of the German Company Law. Latham's proposals are probably more applicable to "outsider systems" of governance with more dispersed share ownership (e.g. the US or the UK).

With regard to Germany one point of criticism would be that the tasks of the monitoring firm are too closely related to those of the supervisory board. In a regime with corporate monitoring firms and supervisory boards, issues regarding the competence and the spheres of responsibility would be pre-programmed. Hence, it would be easier and make more sense to reform the system of the supervisory board than implementing a competing institution operating at the same level. This would most probably invoke the question of power and additionally, the administrative machinery would become inflated and costly.

9.3. Monks

In using a historical method, Bob Monks[577] pleads that true balance of power equilibrium is essential to both the political legitimacy and the economic competitiveness of large corporations.

According to Monks, the development of corporate governance started with the recognition and the consequent separation of ownership and control. This era was followed by what he calls shareholder resolutions and boardroom discussions, meaning the slow emancipation of institutional shareholders. However, he suggests that a new

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575 Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm at -3. Potential Benefits of Monitoring Intermediaries-

576 Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm at -3. Potential Benefits of Monitoring Intermediaries-

577 Monks, Robert A.G. "Relationship Investing" Paper Columbia University, 1993 to download at http://www.lens-library.com/info/colum.html

level called "relationship investing" has to follow these historic developments. This becomes necessary as the existing tools show considerable inefficiencies. Therefore a shift must be made to the extent that the regulatory agencies must take the initiative to enforce the fiduciary obligation of trustees to their beneficiaries. Once a fiduciary standard is created, there is momentum to extending the same duty to other categories like mutual funds, banks and insurance companies.

The Economist sums up what the new models should be able to accomplish:

> "So everything now depends on financial institutions pressing even harder for reforms to make boards of directors behave more like overseers, and less like the chief executives' collection of puppets [...] Financial institutions must also fight to restore their rights as shareholders, lobbying for the dismantling of state takeover restrictions which have provided no protection to workers, only to top managers. Institutions should also demand that shareholder democracy be allowed to operate [...]. But there is more to be done. In the age of the computer, access to shareholder lists should be cheap and simple, not jealously guarded by the boss; that would make it easier to solicit support from other shareholders. Institutions would then be able to use their clout in big firms to elect directors, who would be obliged to represent only their collective interest as owners. Chief executives would still run their firms; but, like any other employee, they would also have a boss. And when they failed at their jobs, they would face the sack"[578].

Getting to the point, he introduces two new structures, which can be designed to bridge the gap between the level of activism that is optimal for individual shareholders (even large ones) and that is ideal for maximum corporate performance.

The first structure involves the corporations adopting by-laws which enable long-term shareholders to monitor the overall direction of the enterprise, "rational involvement" instead of "rational ignorance." This should be achieved by enhanced information passed on to investors (no disproportionate cost or risk) and by their ability to propose solutions to value-inhibiting problems. These so called "long-term shareholders" (who could be defined as those holding a minimum level -- $5 million -- of common shares for a minimum holding period -- three years), in contrast to short term speculators, should be empowered to nominate candidates for a special committee, for approval by all shareholders. Vested with certain powers, the committee should monitor the board of directors and should have access to the company proxy statement for a brief statement of its findings and recommendations. The objective is to allow ownership to be effectively exercised when it is necessary and not to create a "new bureaucracy"[579].

The second structure involves the creation of an investment vehicle specifically created for the sole purpose of monitoring "focus companies." Because owners profit from the

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578 The Economist "Getting Rid of the Boss" 06.02.1993

579 Monks, Robert A.G. "Relationship Investing" Paper Columbia University, 1993 to download at http://www.lens-library.com/info/colum.html at p.25f

existence of an effective governance system, they should be motivated as a class to take appropriate steps to assure that such a system, in fact, is in place[580].

He concludes his findings by the statement:

> "It is increasingly clear that large and regulated institutional investors may be best able to enhance governance through the creation and funding of new entities specially created as effective monitors. Over the last fifteen years since the creation of "index funds," the mode of equity investment by large institutional investors has increasingly become "passive." Instead of buying stock in companies that they think is going to go up and selling stock in companies that they think is going to go down, investors simply buy into a portfolio that replicates the market as a whole, knowing that the likelihood is that the market as a whole will go up (and reflecting empirical data that "active" management has seldom outperformed the market, over time). Indexation has become so popular that it has changed both the way that the market responds to new developments and the way in which trustees view their ownership responsibilities. If a trustee has given up the opportunity to make money (or to send a message to management) by selling the shares, exercising ownership rights is the last chance he has left. He can do nothing and watch an underperforming company sink lower and lower in the index, or he can do something to try to make it do better"[581].

Unfortunately, the suggestions of Monks are only justified from an American angle. Moreover, they are not really topical and show a considerable vagueness, as indicated by an approach which is more of a philosophical nature than of direct reform. Nevertheless, his thoughts are certainly a good basis for improving shareholder-driven corporate governance in Germany. Especially his request for a fiduciary standard is well worth considering as it could certainly serve the effectiveness of the German financial market.

9.4. Mülbert

In his expert's opinion to the 61st Lawyers conference in 1996 Mülbert[582] investigated a number of suggestions. Recognising that the proxy system of the custodians only has a considerably limited abuse potential, he believes that the current situation does not give rise to question the practice as a whole[583]. Nevertheless, Mülbert takes up different proposals to reform the Stock Corporation Act and to scrutinise their perspective.

First, Mülbert discusses the possibilities involving the quantitative restrictions of the interest held by banks[584]. According to his opinion, a reform targeting regulation of the

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580 Monks, Robert A.G. "Relationship Investing" Paper Columbia University, 1993 to download at http://www.lens-library.com/info/colum.html at p.26

581 Monks, Robert A.G. "Relationship Investing" Paper Columbia University, 1993 to download at http://www.lens-library.com/info/colum.html at p.26f

582 Mülbert, Peter „Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?" Gutachten E für den 61. Deutschen Juristentag" Munich 1996

583 Mülbert, Peter „Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?" Gutachten E für den 61. Deutschen Juristentag" Munich 1996 at p. E 75

584 Mülbert, Peter „Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?" Gutachten E für den 61. Deutschen Juristentag" Munich 1996 from p. E 83

interest of banks in stock corporations would be useless. He argues that this does not create an economic difficulty requiring reforms. Mülbert also states that a regulation of the interest would in any case infringe the Equality Principle in Art. 3 Grundgesetz. Hence, regulation of the interest is not an option. Nevertheless, the crossholdings by big insurance companies and banks are on trial at present, as a number of restructuring initiatives indicate (e.g. Deutsche Bank selling off Daimler Chrysler shares).

Additionally, Mülbert investigates the proxy voting practice and possible reforms of the system. Fortunately, his major point of concern with the proxy voting practice of the custodians, § 128 s.2 s.2 AktG, was altered by Art. 1 No.10 a NaStraG in 2000. Therefore his arguments became diluted.

9.5. Bill by the Social Democrats and Suggestions by Baums/von Randow

During the Nineties, the Social Democratic Party[585] presented two concepts. The first one was based on proposals by Baums and von Randow[586]. The second concept was more advanced and resulted in a bill. Both suggestions to reform the system were based on the same approach. Therefore it is advisable to scrutinise the theories in cumulo.
Both hypotheses provide that custodian banks are only entitled to function as proxies if single instructions by the shareholder are given. Here the role of custodian banks is taken over by five shareholder representatives, who should be elected for five years (SPD), as well as two to three voting administrators elected for three years (Baums). From today's point of view it is incomprehensible that those agents should be provided by the auditors as a conflict of interest would be programmed.
The elected representatives should compete against each other for the shareholders' ballots. This contest should guarantee a qualitative selection.
There is a difference regarding the scope of the voting rights. While the bill of the Social Democrats provides that the shareholder representative is only entitled to vote for the delegated proxies, the voting administrator should represent those shareholders who were not interested in voting. The agents should be compensated (by the company) according to the number of shares they represent.

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585 Gesetzesantrag des Landes Rheinland-Pfalz „Entwurf eines Gesetzes zur Steigerung der Effizienz von Aufsichtsräten und zur Begrenzung der Machtkonzentration bei Kreditinstituten infolge von Unternehmensbeteiligungen"
1997 (BR-Drucksache 561/97) to download at
http://www.parlamentsspiegel.de/WWW/Webmaster/GB_I/I.4/Dokumentenarchiv/dokument.php?k=BBD561/97, a critical comment to these alterations compared to his own suggestions could be found in Baums, Theodor „Vollmachtsstimmrecht der Banken - Ja oder Nein?" Universität Osnabrück, Institut für Handels- und Wirtschaftsrecht, Paper No. 29, 1995 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm at p.25 ff
586 Baums, Theodor/von Randow, Philipp „Der Markt für Stimmrechtsvertreter" in Die Aktiengesellschaft Volume 40, 1995 p.145-163

Criticism[587] is certainly appropriate regarding the representatives. It is not advisable to choose auditors, not only due to the experience made with Enron and Worldcom. Their conflicts of interest are omnipresent. Moreover, the requirement of a single instruction would most probably lead to a further decrease of the capital presence.
Furthermore, the "politicising" of the general meeting towards a "shareholder parliament" might be a good idea at first glance, but problems are undoubtedly inherent. The creation of such a system would probably lead to an unwanted polarisation in the general meeting, populist representatives and over-regulation.
In addition to that, the compensation model is not able to guarantee quality (good corporate governance). The payment by the company will again lead to a conflict of interest of the agents.
To draw a conclusion, it has to be acknowledged that the legal development has superseded these theories. Now, not only possibilities exist like voting via the internet or handing over the completed ballots to company representatives, but also obligations, which state for instance that investment trusts should vote for their funds by themselves, or can use an independent proxy.

9.6. Enhancing the Role of Shareholder Associations

It is well worth having a look at the shareholder associations[588]; especially as their role is mentioned in § 135 s.9 no.1 AktG. But the question arises if they are really capable of playing an alternative role to custodian banks. It should be possible to say that they are free from any conflict of interest as they are financed by contributions of their members. Their role began to be questioned because of the suspicion of insider trading and financing by stock corporations in some recent crisis[589]. Moreover, their influence is limited as they rarely represent more than one percent of the votes in the meetings. Therefore the shift towards shareholder associations has to be enormous. As a consequence it has to be doubted whether they are prepared and determined to take on such an organisational challenge.
Additionally, their structure as an association will complicate efforts of opening them up to other shareholder groups. Financing needs to come from earnings of offered services and other products instead of membership fees. Furthermore, the articles of association would require a reform away from non-profit orientation towards a profit orientated organisation.

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587 In detail Tuerks, Robin „Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.44 ff or Mülbert, Peter in „Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?" Gutachten E für den 61. Deutschen Juristentag" Munich 1996 at p.E92 ff

588 The two most popular in Germany are the Deutsche Schutzvereinigung für Wertpapierbesitz (www.dsw-info.de) and the Schutzgemeinschaft der Kapitalanleger (www.sdk.org).

589 Jakobs, Georg/Schmitt, Jörg „Etikettenschwindel" in Manager Magazin 10/02 p.206ff

However, a big obstacle will also be their reputation as activists. This flaw, whether it is justified or not, will repel a number of investors (especially institutional investors).
On the other hand it has to be mentioned that their influence will certainly increase with the retreat of the custodian banks. In order to avoid an unwanted cooperation with another bank or asset management (fear of disclosure), a solution might be sought, which might include voting via the associations.

9.7. Limited Voting Right

Tuerks[590] remarks that the limitation of the voting right, as § 3 s.5 s.1 VW-Privatisierungsgesetz provides for the Volkswagen AG, might be an approach to reduce the influence of custodian banks. However, limiting the voting rights would certainly result in a low capital presence[591], which would be far below the current turn-out. Therefore this suggestion cannot be acceptable. Reforms should result in an increase or at least a stabilisation of the capital presence and avoid the creation of accidental majorities.

9.8. Requirement of Single Instructions

The "Bankenstrukturkommission[592]" (Commission on the Structure of Banks), appointed by the Ministry of Finance to solve fundamental questions of the credit service sector, suggested to demand single instructions for decisions requiring a qualified majority and for the election and the discharge of members of the supervisory board employed by a custodian bank.
Logic predicts decreasing turn-out at meetings. Voting would simply become too complicated and expensive. In addition to that, the already existing enormous administration with proxy voting would be further inflated.

9.9. The Bank Employed Proxy Agent

A questionable reform is the suggestion to introduce bank-employed proxy agents[593] to vote free of instructions and independently. It is suggested that they should function as the "bad conscience" of the custodian bank. In addition to that, this reform should enhance transparency.

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590 Tuerks, Robin „Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000

591 Presence number in the general meeting of the Volkswagen AG 2004: 37,21 %

592 Bericht der Studienkommission (Bankenstrukturkommission) „Grundsatzfragen der Kreditwirtschaft", Bonn 1979 at p.993f.

593 Sabine Leutheusser-Schnarrenberger „Im Kräftefeld der Interessen: Das Vollmachtsstimmrecht der Banken" in Der Betrieb (DB) 1995 at p.2355

In general, this approach could be able to take the proxy voting process away from the banks at least to some extent. Nevertheless, it is more than doubtful that a proxy agent paid by the bank will be independent from it. To push the criticism further, a bank-employed proxy agent would probably not be more than a puppet. Even if the bank will not influence him the agent is not safe from trying to act in the interest of his employer[594]. Hence, this reform is not acceptable as it pretends independence where there is none.

9.10. "Voting Mandatory"

A reform suggested by the Bundesrat aimed at the introduction of a "Voting Mandatory[595]". The idea of "mandatory" was the logic conclusion from a restriction of the voting right of the custodian banks[596]. The Bundesrat saw an increasing demand for independent proxy agents as an alternative to the custodian banks. As the "mandatory" was seen as a new profession, with a very responsible assignment, the Bundesrat suggested to require personal qualifications supervised by the Bundesaufsichtsamt für Wertpapierhandel (today BAFIN - Bundesanstalt für Finanzdienstleistungsaufsicht).
It cannot be denied that this bill by the Bundesrat included some advanced innovations. From today's point of view it was certainly sensible to agree on introducing a new group of proxies (Just referring to the proxy committee of the stock corporation in § 134 s.3 s.3 AktG). In addition to that the required personal qualifications will most probably come up again in conjunction with § 32 s.1 s.4 InvG[597].

However, criticism of this bill is certainly unavoidable. The main problem attached to this initiative is the accompanying overregulation[598]. It is more than questionable if an overloaded supervisory authority would be able to cope with the control of the suggested amendments and to cover the increasing costs. Furthermore, it has to be expected that the restrictions of the voting right of the custodian banks will result in further decreasing capital presence. This could partly be seen as a result of increased regulation (Which proxy does represent my interests best?) and the missed opportunity

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594 Same criticism: Baums, Theodor „Vollmachtsstimmrecht der Banken – Ja oder Nein?" Universität Osnabrück, Institut für Handels- und Wirtschaftsrecht, Paper No. 29, 1995 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm at p.19, 20

595 Gesetzesantrag des Landes Rheinland-Pfalz „Entwurf eines Gesetzes zur Steigerung der Effizienz von Aufsichtsräten und zur Begrenzung der Machtkonzentration bei Kreditinstituten infolge von Unternehmensbeteiligungen" 1997 (BR-Drucksache 561/97) to download at http://www.parlamentsspiegel.de/WWW/Webmaster/GB_I/I.4/Dokumentenarchiv/dokument.php?k=BBD561/97
- Alteration regarding § 135 s.9 s.3 AktG

596 Alteration regarding § 135 s.1 AktG – the Bundesrat suggested to couple the voting right with its role as a creditor within the stock corporation and to avoid the accumulation of own voting rights and proxies.

597 It would be surprising, if the BAFIN (Bundesaufsichtsamt für das Finanzwesen - German supervisory authority) would refrain from regulating and defining the role of "someone".

598 Tuerks, Robin in „Depotstimmrechtspraxis versus U.S.-proxy-system: der Beitrag von Finanzintermediären zur Optimierung der Unternehmenskontrolle" Munich 2000 at p.52

to make the voting process easier. The question of the agency costs also remains unsolved. Regarding the institutional investors it could be assumed that they will be prepared to pay for this proxy service. However, this cannot be expected from private investors. Most probably they will not be ready to take over the administration costs.

In drawing a conclusion to this bill, it should be stated that it appears promising. Installing an authority as an alternative to the custodian banks is certainly the right approach. However, the legislator should promote the idea of the "mandatory" and provide incentives for using one rather than producing another law producing additional administration.

9.11. Bonus for Exercising the Vote

The suggestion that shareholders who executed their voting right should receive the incentive of a higher dividend (10-20%)[599] to increase the turn-out at annual general meetings can be supported. Nevertheless, this idea should not become a legal requirement and should be left dispositive to the statutes of the company[600]. This solution would provide far more flexibility as the companies could decide by themselves whether this tool is necessary and under which conditions it should operate[601]. By introducing a bonus for exercising the vote, the company will not only give an incentive to those shareholders using their voting right and thus lower the danger of accidental majorities, but it will also pay the governing costs and consequently, foster shareholder engagement. It is recommendable that the bonus should be paid to the shareholder who is eligible to vote at the general meeting (day of the record date) and not to the shareholder who acquired the shares after the record date but before the general meeting[602].

The question of hidden representation, that is only the proxy is known and not the shareholder (e.g. in the case of bearer shares), could turn into a problem. As such a verification process is complex and could be costly[603], the economical feasibility comes into focus. Doubts on the idea of the bonus also arise regarding the amount of the

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599 Davis, Stephen, "Voting Pays" in Global Proxy Watch; Vol. IX No. 35; 7. Oct. 2005, 599; Klühs, Hannes „Präsenzboni für die Teilnahme an der Hauptversammlung - Ein Vorschlag zur Steigerung der Hauptversammlungspräsenz bei Aktiengesellschaften" 2005; Paper No.124 to download at http://publikationen.ub.uni-frankfurt.de/volltexte/2005/2335/pdf/124Aufsatz_prn.pdf

600 Deutsche Schutzvereinigung für Wertpapierbesitz „Hauptversammlungssaison 2005" to download at http://www.dsw-info.de/Hauptversammlungssaison_2005.566.0.html

601 Klühs, Hannes „Präsenzboni für die Teilnahme an der Hauptversammlung - Ein Vorschlag zur Steigerung der Hauptversammlungspräsenz bei Aktiengesellschaften" 2005; Paper No.124 to download at http://publikationen.ub.uni-frankfurt.de/volltexte/2005/2335/pdf/124Aufsatz_prn.pdf at p.5

602 Klühs, Hannes „Präsenzboni für die Teilnahme an der Hauptversammlung - Ein Vorschlag zur Steigerung der Hauptversammlungspräsenz bei Aktiengesellschaften" 2005; Paper No.124 to download at http://publikationen.ub.uni-frankfurt.de/volltexte/2005/2335/pdf/124Aufsatz_prn.pdf at p.9

603 Davis, Stephen, "Voting Pays" in Global Proxy Watch; Vol. IX No. 35; 7. Oct. 2005

premium to be paid. Although a 100% capital presence can not be expected it needs to be taken into consideration. This also provides an element of uncertainty. However, a solution to this latter problem might be to expect 100% capital presence and to define a fixed bonus which will be paid out. This premium could then be distributed among those who are actually physically present. To give an example: The company announces a 5 Cent bonus for exercising the voting right. When only 50% of shareholders make use of their right, then their premium will raise to 10 Cent.
The success of this suggestion depends on a calculation of the expenses. However, the suggestion of a bonus for exercising the vote is supported by the Spanish financial market where payments for the execution of the vote of two to ten Cents per share on the dividend lead to increased capital presence (E.g. Endesa rose from 37% to 66%)[604].

I shall argue that the "educational" approach is certainly problematic. The investor should cast his vote because he is convinced that governance matters, which will in exchange foster shareholder value, and not because he is paid for it. Stock picking in order to claim the dividend bonus will certainly increase the capital presence but does not automatically serve good governance and does not avoid corporate scandals.

To draw a conclusion, a bonus payment for shareholders casting their vote is a proactive and elegant suggestion to overcome the constant decrease of turn-out numbers at general meetings and to improve the engagement of investors. If this approach could have enough economical substance will be shown by the interest of the financial market.

9.12. Further Suggestions

Because of the renunciation of some of the custodian banks, a number of further suggestions became almost superfluous. Worth mentioning in this respect are transparency and publication rulings as well as renunciations with respect to decisions where a conflict of interest might arise[605]. Moreover, fundamental demands like the abolition of the custodian voting right[606], as Wenger suggests, or the sale of preference shares solely to small private shareholders[607], according to Müller-Erbach are once and for all off the agenda. Instead of an additional reduction of the voting right of custodian

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604 Klühs, Hannes „Präsenzboni für die Teilnahme an der Hauptversammlung – Ein Vorschlag zur Steigerung der Hauptversammlungspräsenz bei Aktiengesellschaften" 2005; Paper No.124 to download at http://publikationen.ub.uni-frankfurt.de/volltexte/2005/2335/pdf/124Aufsatz_prn.pdf at p.4

605 Mülbert, Peter „Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?" Gutachten E für den 61. Deutschen Juristentag" Munich 1996 from p. E 100

606 Wenger, Ekkehard „Stellungnahme zur Aktienrechtsreform" Die Aktiengesellschaft - Sonderheft, August 1997 from p.57

607 Müller-Erzbach, Rudolf „Umgestaltung der Aktiengesellschaft zur Kerngesellschaft verantwortungsvoller Großaktionäre" Berlin 1929 at p.20ff

banks it should be more desirable to maintain at least some influence by custodian banks. With regard to the current situation and some of the suggestions mentioned above, it has to be acknowledged that the custodians might be the only institution which is prepared to offer reasonable proxy voting to private investors. Moreover, it has to be kept in mind that the custodians also function as an opinion-forming body in corporate policy.

9.13. Notions on the Further Development

The landscape of Company Law has changed considerably over the last years. A huge wave of reforms has created a completely different scenery. Today the discussion on how to deal with custodian votes has been almost eliminated. Less fundamental issues like the development of proxy voting, the driving back of the co-determination in the supervisory board or the purification of the annual general meeting, are now in the limelight of reforms. As the presentation of the UMAG already suggests in this "post-custodian period", ground-breaking reforms cannot be expected. Company Law will probably be reformed permanently instead. This means that small steps will be taken to enhance shareholder engagement. Yet it cannot be expected that the activity of the legislator will slow down. The still existing shortcomings in the law and the changing environment of shareholder engagement will guarantee a further development of reforms.

10. Chapter: Conclusions: Three Proposals for the Improvement of Shareholder Engagement

Shareholder engagement is a load-bearing pillar in the German corporate governance system. Not only does it support transparency and control of stock corporations but it also serves as a value-enhancing factor, as demonstrated in previous chapters. The environment for the investor to become active has changed considerably over the last couple of years. Reason for this development was an increased sensibility towards shareholder issues not only by the legislator but also by the companies. Now the investors are not longer regarded as simple sponsors of the company. They have become emancipated.

Nevertheless, although considerable progress has been made, there is still considerable room for improvement. Therefore, I will point out three areas of shareholder engagement where I think that a reform approach will have a positive effect on the German corporate governance regime.

10.1. Path Dependency as a Condition

Condition for a sound reform of Company Law is that the alterations are "path dependent". In explaining this approach Cheffins has argued that ""law matters" in the sense that laws, which allow investors to feel confident about owning a tiny percentage of shares, constitutes the crucial "bedrock"" [608]. Therefore, legal reforms should follow the existing legal path and consider the legal status of the shareholder. Although his inquiry was mainly based on economies dominated by widely held public companies, his findings are even more valid with regard to regimes where ownership is primarily concentrated. The assumption that dispersed share ownership can only arise if a country's legal system provides strong shareholder protection for minority shareholders has important normative implications[609]. In other words, the various market-orientated factors offering protection to investors in fact proved highly effective in mobilising capital and assuaging perceptions of risk[610]. Legal reforms of moderation, which do not only take the existing legal and financial but also the social environment into account, could foster share ownership and the financial market as a whole in Germany. Especially with regard to the struggling pension system and an economic

608 CHEFFINS, Brian R. „Law as Bedrock: The Foundations of an Economy Dominated by Widely Held Public Companies", in Oxford Journal of Legal Studies, Vol. 23, No. 1 (2003) p. 1-23

609 CHEFFINS, Brian R. „Law as Bedrock: The Foundations of an Economy Dominated by Widely Held Public Companies", in Oxford Journal of Legal Studies, Vol. 23, No. 1 (2003) p. 1-23 at p.7

610 CHEFFINS, Brian R. „Law as Bedrock: The Foundations of an Economy Dominated by Widely Held Public Companies", in Oxford Journal of Legal Studies, Vol. 23, No. 1 (2003) p. 1-23 at p.12

stability path dependency for the future, development of shareholder engagement is crucial.

Having pointed out the importance of the "law matters" theory, the shortcomings hindering a sound development of the shareholder engagement hierarchy need to be pointed out. Primarily three unsolved issues have to be mentioned in this respect: The question of financing shareholder engagement, the unawareness and reluctance of investors, and shortcomings in the Company Law.

10.2. First Proposal: Financing Shareholder Engagement

As long as investors have to cover the costs for engagement they are reluctant to pursue their rights listed in the hierarchy of shareholder engagement. Even provisions in the law (just mentioning § 32 s.1 s.3 InvG, which states that Kapitalanlagegesellschaften should vote their national stock) do not provide the necessary basis to become active. Having said this it should be mentioned that shareholder engagement is quite costly, considering the fees for hiring a proxy voting service or lawyer, sending a representative to the general meetings, proxy fights, administration, inquiries or analysing the company, etc..
Mostly institutional investors intending to become active, be it at the general meeting or through shareholder negotiations with management, have to carry the accompanying costs. Other investors profit from their engagement not only as they do not need to become corporately active themselves, but also because they could benefit from the improved performance. Consequently, this issue is called the free-rider problem.

The active Kapitalanlagegesellschaft can use the performance to promote its fiduciary responsibility. *Deutsche Bank* investment subsidiary *DWS* and *Union Investment* are good examples, which often attract attention at general meetings and hence the media, by criticising or praising deeds of management. The same is true for shareholder associations like the *Deutsche Schutzvereinigung für Wertpapierbesitz* (DSW) or the *Schutzvereinigung für Kapitalanleger* (SDK). However, the costs involved in executing good corporate governance could be extraordinary for an investor. It certainly has to be admitted that due to the custodian banking system in Germany the problem of agency costs was not a primary concern[611], as corporate governance was pursued and financed by banks. However, the situation has changed. It has to be acknowledged that since the custodians have pulled out of the proxy voting business, or at least have reduced their

611 Jürgens, Ulrich/Rupp, Joachim/Vitols, Katrin/Jäschke-Werthmann, Bärbel "Corporate Governance und Shareholder Value in Deutschland" - Veröffentlichungsreihe der Abteilung Regulierung von Arbeit des Forschungsschwerpunkts Technik-Arbeit-Umwelt des Wissenschaftszentrum Berlin für Sozialforschung FS II 00-202, 2000 to download at http://bibliothek.wz-berlin.de/pdf/2000/ii00-202.pdf at p.7

services in this area, capital presence at general meetings has decreased and the free-rider problem has become more of an issue. This is illustrated by the fact that some institutional investors, like *dit/ADAM, CSAM* or *Invesco Asset Management* and others, have out-sourced their voting to a proxy voting service, while other firms try to maintain voting via the custodians, or simply prefer not to vote at all. Private shareholders now prefer to renounce their vote instead of paying fees for its execution, or going to the trouble of finding other ways to vote (e.g. custodians that are still active, shareholder associations, investment clubs, proxy committees etc.). Equally, global shareholders face difficulties and high costs when they try to pursue informed voting abroad. Hence, they prefer not to cast their vote.

Following the hierarchy of shareholder engagement, I only see voting to have a serious possibility to be financed by the company and not by the shareholder. The other forms of engagement are already financed by the company (information material, shareholder proposal (§ 122 s.4 AktG), calling a meeting (§ 122 s.4 AktG)), do not carry considerable costs (speaking at the meeting) or are not sufficiently transparent (shareholder negotiations). Moreover, the shareholder who intends to file a suit could ask for legal aid (§ 247 s.2 AktG).

To solve this free-rider problem, the following proposals can be taken into consideration for reforms to the financing of corporate governance existing so far.

10.2.1. Duty of Loyalty

One way of avoiding the free-rider problem might be through the shareholder's duty of loyalty. This might be so if such a duty had a horizontal effect. Having said that, the shareholder could engage when there is an under-performance of the company with the result that a compensation of his costs might be possible via joint liability. However, the duty of loyalty is only applicable in cases of unacceptable conduct in the market, endangering shareholder assets and disloyal behaviour at elections by a company. When the under-performance is related to these cases, then compensation for shareholder engagement via this construct is possible. Not justifiable for an expense allowance via the duty of loyalty is the mere under-performance in contrast to comparable companies.

10.2.2. Making Voting a Legal Obligation

Currently, Kapitalanlagegesellschaften are only supposed and do not have to vote (§ 32 s.1 s.3 InvG). This situation is quite unsatisfactory as, on the one hand Kapitalanlagegesellschaften do not feel obliged to vote, while on the other hand the supervisory authority cannot sanction this failure to comply and hence, cannot see the necessity to act. Reforming this act and exchanging this "should vote" provision with a

"must vote" provision will improve the awareness and certainly the voting engagement. With reference to (still) a number of custodians, the proxy committees or intermediaries, who function as proxies, the institutional investor has sufficient tools to pursue a responsible voting policy. Whatever solution the shareholder chooses he will incur the selected agency's costs. However, while Kapitalanlagegesellschaften carry the cost for executing the votes; private, corporate and other shareholders will not be involved in this financing issue. Where voting has been made compulsory for funds, like in the US or Spain, this legal obligation has at least been able to weaken the free - rider problem. Unfortunately, § 32 s.1 s.4 InvG has recently been changed by the 4. Finanzmarktförderungsgesetz. Hence, it is debatable whether the legislator will review the document with respect to an alteration of § 32 s.1 s.3 InvG in the near future.
However, it needs to be pointed out that the Bundesanstalt für Finanzdienstleistungsaufsicht (BAFIN - supervisory authority) was given means to supervise the performance of the Kapitalanlagegesellschaften. An infringement of the "should vote" provision could be sanctioned. But as this formulation is pretty vague and the BAFIN does not see voting as an important issue on their agenda and prefers a solution by the market[612], it cannot be expected that a change will come from this side.

10.2.3. The Intermediate

Another option is to promote the use of an intermediate offering proxy voting as well as corporate governance analysis of companies. Certain authors[613] have developed different theories regarding the concept of intermediates. These authors concluded that establishing the use of intermediates would have the capacity to reduce agency costs that emerge from shareholder engagement.

10.2.3.1. The Corporate Monitoring Firm

The theory of Mark Latham on the corporate monitoring firm has already been explained in the previous chapter. This theory provides a solution to avoid the free-rider problem. The issue is that the corporate monitoring firm is too closely related to the supervisory board. Hence, with regard to the question of financing corporate governance, it has to be questioned if shareholders would be prepared to cover the costs for the corporate monitoring firm.

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612 Statement of the Chairman of the BAFIN, Jochen Sanio, at a speech held at the American Chamber of Commerce in Stuttgart (5th of April 2006)

613 E.g. Latham, Mark „The Corporate Monitoring Firm" in Corporate Governance - An International Review January 1999 (Volume 7 No. 1) and at www.corpmon.com/CorpMonFirm.htm and Baums, Theodor „Vollmachtsstimmrecht der Banken - Ja oder Nein?" Universität Osnabrück, Institut für Handels- und Wirtschaftsrecht, Paper No. 29, 1995 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm at p.25 ff

10.2.3.2. Baums

A similar view was stated by Theodor Baums in 1995[614]. He pleads for the involvement of professional proxy agents, as they require only one payment for all services. This is an economically sensible solution since the proxy agent has considerable specialisation and dimensional advantages with regard to procurement and evaluation of enterprise-relevant information. However, to guarantee a qualitatively convincing service, proxy agents have to meet some requirements[615]:
-independence between the proxy agent and the stock corporation
-guarantees that the proxy agent does not pursue extraneous aims
-the pricing model of the proxy agent has to avoid the free-rider effect
-the proxies have to guarantee effective control at the general meeting

One important consequence is that certain qualitative and quantitative standards must be maintained. Therefore, Baums supports the view that shareholders who are unable to be present at the general meeting should be represented by a qualified "proxy administrator" elected by the general meeting. However, it has to be recognised that this opinion was accompanied by the omnipotent role of the banks at that time (1995) and was aimed at reforming the custodian system. This problem is currently not as relevant and therefore should be put into perspective. Nonetheless, this opinion provides an approach as to how the agency costs could be divided among a number of shareholders with the result that the free -rider problem is somewhat diminished.

10.2.3.3. Agency without Authority

In contrast to the Anglo-American legal system, in the German and probably also in the Roman and Middle-European one, it is possible to dissolve the free-rider problem via the construct of an agency without authority according to § 677, 683s.1 BGB. Not only is this solution elegant but also simple, as no reform of the existing Company Law is necessary.
Conditional for Germany in this respect is that the votes are not distributed via the custodian but by a proxy voting service directly. The Decree on the indemnification on custodian expenses (Verordnung über den Ersatz von Aufwendungen der Kreditinstitute 2003) is closing, which means that custodians cannot ask for an additional indemnification (e.g. voting) than for sending out AGM materials on behalf of the custodian.

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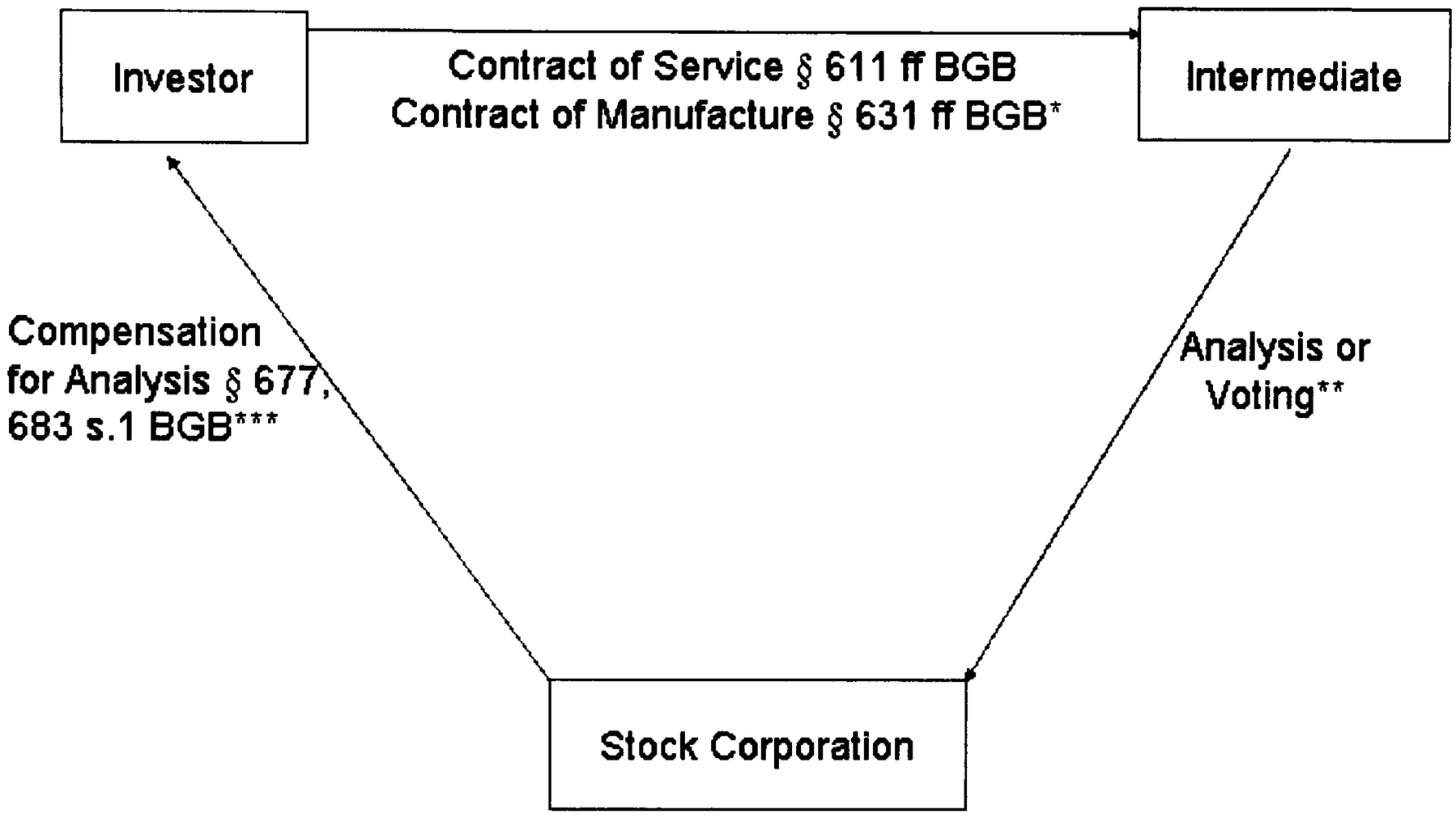
614 Baums, Theodor/von Randow, Philipp „Der Markt für Stimmrechtsvertreter" Working Paper No.22 1/1995 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm

615 Baums, Theodor/von Randow, Philipp „Der Markt für Stimmrechtsvertreter" Working Paper No. 22, 1/1995 to download at www.jura.uni-osnabrueck.de/institut/hwr/papers.htm at p.21 ff

The concept is based on a triangle between an intermediary, the institutional investor and the company. This avoids a conflict of interest because there is no contractual basis between the intermediary and the company. The intermediary is paid for his services by the investor, who has the legal tool to claim back these payments from the company.

Figure 27: Agency without Authority Triangle



* A contract of service according to § 611 ff BGB, a contract of manufacture according to § 631 ff BGB, or a combination of both (as might occur in a consulting contract, when the drawing up of a written expert's opinion likewise is a determining element of performance[616]) needs to be closed.
**There is no contractual relationship between the intermediary and the company. This is necessary to avoid conflicts of interest.
***Basis of claim for the compensation of the costs, which arise from the contract between the investor and the intermediary, is an agency without authority according to § 677, 683 s.1 BGB.

The condition for an agency without authority according to § 677, 683s.1 BGB and hence, for a compensation of the agency costs is (1) a conduct of business, which the (2) outside executive conducts, (3) with the will to manage another one's business, (4) without being authorised or entitled. Additionally, (5) the conduct of business has to be in the interest of the principal.

(1) Taking the diagram above as the solution scheme, the contract between investor and intermediary has to be a conduct of business. This condition is met when the activity is of legal or real nature. The conduct of business is also covered when the executive chooses a third party to conduct the business[617]. The contract which is made between

616 „J. von Staudingers Kommentar zum Bürgerlichen Gesetzbuch" 13th Edition Berlin 1995 at § 675 C117 (Martinek)

617 Dörner, Heinrich /Ebert, Ina/Eckert, Jörn/Hoeren, Thomas/Kemper, Reiner/Schulze, Reiner/Staudinger, Ansgar „Bürgerliches Gesetzbuch" Baden-Baden 2001 at § 677 No.2 (Schulze)

investor and intermediary/proxy voting provider is a conduct of business and thus fulfils the required condition.

(2) Moreover, the business has to be conducted by an outside executive. Providing that the intermediary does not have any contractual relations with the investor, he is an outside executive.

(3) A further requirement is that the outside executive has the intention to manage the business of a third party. Two reasons for the formation of the contract between the investor and the intermediary can be determined. Firstly, contracting between the intermediary and the company might lead to conflicting interests and is therefore inappropriate. Secondly, the custodians gradually abandon the proxy voting business and are often unable to provide a global proxy distribution. Issuers do not and strategically cannot offer a suitable replacement providing sufficient coverage. Therefore the outside executive has the intention to manage the business of a third party.

(4) The investor does not need to be authorised or entitled by the company. Providing the company's articles of association state otherwise, the shareholders are generally not entitled or authorised, by the company to hire an outside service. This is also valid with regard to voting via an authorised proxy.

(5)Finally, the conduct of the business has to be in the interest of the company. In general, companies want to avoid accidental majorities, see their investors selling the shares and maintain the shareholder rights granted by the Stock Corporation Act. These shareholder rights indicate that the investors should be comprehensively informed about the business of the company and have the right to get involved in the general meeting. The right to file an action needs to be excluded as it is for obvious reasons not in the interest of the company.
Often enough the mentioned shareholder rights can only be executed with difficulties. Such difficulties arise for example for shareholders from abroad who might receive an agenda in a foreign language, or whose custodian charges enormous fees for executing the vote (e.g. Italy up to 600 Euro/meeting) if at all. Local investors might have difficulties executing their shareholder rights as well, considering that a number of German custodians have pulled out of the proxy voting business.
Consequently, the company has an alleged interest that investors hire an intermediary to help overcoming these problems.

Important to mention is that the conduct of business does not need to be successful. § 677 BGB only demands conscientious implementation of the business that has been taken over and not the realisation of success[618].

Following the approach of the agency without authority the free-rider problem seems to become obsolete. As the corporation pays compensation to the investor, all shareholders are under equal financial strain. A conflict of interest is avoided, as the intermediary is not dependent on the company, but is exclusively paid by, and only responsible to, the investor. This gives intermediaries additional possibilities in pursuing corporate governance.
Finally, this construct does not require initiative from the legislator, since the possibilities of existing laws are exhausted, so lengthy discussion with a subsequent legislative procedure is superfluous. The shareholder could even seek compensation ex tunc (§ 95 BGB limitation 30 years).

Having shown the possibility of circumventing the free-rider problem, it is interesting to see how the solution could be realised. The critical point is to create an interest by the company, which will consequently address the issue of finance. The following research path is conceivable:
1. Consulting contract between the investor and the intermediary.
2. The intermediary will seek dialogue with the company:
a) Is the company prepared to accept such a foundation of a claim?
b) What will be the scope of compensation?
c) How can floodgates for other intermediaries be avoided?
d) Will the corporation be open for dialogues if the intermediary provides suggestions for improvement?
3. The results and suggestions will be presented to the investor.
4. The intermediary will receive a mandate to outline the conditions with the company
5. The investor will claim the charges he or she paid to the intermediary from the company

Concluding, it is important to point out that if the market participants agree on the "agency without authority" construct then not only corporate governance in Germany could be improved, but also the relationship between the stock corporation and its investors.

618 „J. von Staudingers Kommentar zum Bürgerlichen Gesetzbuch" Berlin 1995 13th Edition at § 677 No.8 (Martinek)

10.3. Second Proposal: Overcoming the Lack of Awareness and Apathy of Shareholders

It is quite unsatisfactory that the vast majority of investors do not sufficiently know their shareholder rights and how to adequately pursue them. Moreover, when looking at the capital presence at general meetings it could be concluded that there is even apathy towards the execution of shareholder rights. The fact that even institutional shareholders ignore their fiduciary duties is a serious issue.
These shortcomings prevent sound shareholder engagement according to the claimed hierarchy and weaken corporate governance from the shareholders' side.
While other forms of engagement are not sufficiently transparent (negotiations) or are less of an issue to allege a lack of awareness (e.g. information request, shareholder proposal or calling the meeting), the apathy and the lack of consciousness become quite obvious with regard to voting (especially cross-border).
In contrast to that, the right to file a suit has been used excessively in the past[619], which shows that shareholders are quite aware of this tool.

To overcome these shortcomings German companies had improved "shareholder education" considerably in the last couple of years. However, to further enhance their relationship with investors they need to implement the new possibilities provided by Company Law rigorously, in particular with regard to improved usage of the Internet. Here especially the electronic distribution of reports, ballots and other material needs to be emphasised again. It is also necessary for companies to acknowledge the growing number of foreign shareholders. They should receive an annual report and an agenda of the general meeting in German and English. The fewer obstacles there are for an investor to participate in a general meeting and to inform himself, the more likely it is that he gets involved in corporate policy and thus in corporate governance.
Regarding the "education" of institutional investors, the German Association of Investment and Asset Management (BVI), has not yet exhausted its possibilities. In any way it is important to point out that the BVI has recognised the importance of an informed voting. To encounter the reluctance of institutional shareholders the BVI offers its members a general meeting service which provides announcement and analysis of 220 German and European meetings. This service started in 2007.
Although private shareholders cannot and should not be obliged to execute their vote, this is not necessarily the case for institutional investors, especially as they have a fiduciary responsibility towards their clients. The key section with regard to voting is § 32 s.1 s.3 InvG. When the legislator changes the provision so that Kapitalanlagegesellschaften have to execute their votes (currently they should execute them), they are urged to take their fiduciary responsibilities more seriously with the

619 Chapter 6.2.6

result that the safeguarding of shareholder rights would become a quantifiable value. Here it should be added that an active fund might also function as a positive example for enhanced engagement of private shareholders. Although a further legal obligation should be the last option for the legislator, the capital presence and the behaviour of the fund industry show that an alteration of § 32 s.1 s.3 InvG towards compulsory voting is almost unavoidable.

The issue of voting could be quite complex. Therefore, it is necessary that investors use the services of intermediarys to overcome shortcomings in the pursuit of shareholder rights. This will not only save them administrative work, but will also enhance their sphere of action, while strengthening corporate governance in general. Equally important in this respect is the introduction of a voting policy by institutional shareholders as the voting process could be automated. The use of such a policy will reduce the workload in the proxy season and will be an indicator for the issuer when drawing up the general meeting agenda.

10.4. Third Proposal: Correcting Shortcomings in Company Law

The third area where shareholder engagement could be improved is Company Law. Although it has been considerably reformed by the legislator, a number of issues still need to be solved.

To start with, the issue of transparency for better shareholder information needs to be addressed. The Security and Exchange Commission in the US requested "Disclosure, again disclosure and yet more disclosure"[620]. This statement is also valid for Germany. Although the legislator introduced the new VorstOG - Vorstandsvergütungs-Offenlegungsgesetz (Management Remuneration Disclosure Act) 2006[621] to increase the disclosure requirements regarding the remuneration of the management for companies, it needs to be recognised that certain transparency provisions are still in need of further development. To mention in this respect are for instance accounting standards, an area in which some companies still have to catch up.

Some reforms to improve shareholder engagement in the general meeting have been introduced by the UMAG. At this point, however, it is too early too assess if they are adequate means of enhancing issues like speaking at the general meeting or voting.

The right to file a suit according to § 243 AktG is certainly still in need of reform. It has to be acknowledged that some improvements have been made by the UMAG in 2005. However, as it has been stated above, it is essential to recognise the entrepreneurial risk

620 Noack, Ulrich „Modern Communication Methods and Company Law" at B I, to download at http://www.jura.uni-duesseldorf.de/dozenten/noack/texte/noack/eblr.doc

621 Gesetzentwurf der Bundesregierung „Entwurf eines Gesetzes über die Offenlegung der Vorstandsvergütungen (Vorstandsvergütungs-Offenlegungsgesetz – VorstOG)" to download at http://dip.bundestag.de/btd/15/055/1505577.pdf

for stock corporations. This could be endangered by law suits. It should be down to the management board, the supervisory board and the general meeting, for example, to decide on a takeover and not to the courts. I pointed out that strengthening the judgement procedure will not only benefit the company as its resolutions will not be blocked, but it will also improve the possibility of the shareholders to claim compensation and ease the workload of the courts. Only in cases of severe damage threatening the company the filing of an action should be made possible.

Beyond the hierarchy of shareholder engagement, the structure of the supervisory board (codetermination of employee representatives, former CEO on the board) is in need to reform. It is not necessary to question the two-tier board system as a whole as the supporters of such a solution recommend, though the conversion of the Societas Europea into national law needs to be observed. From my point of view a complete reconstruction of the board system will lead to deterioration of corporate governance at least for the transitional period. It would be better to improve the standard of the supervisory board than to fundamental changes. It is certainly easier not to allow shareholder representatives who have more than five mandates or former members of the management board to be put on the list of candidates than to introduce a single board system.

Having stated the request for an improved legislation, it is necessary to emphasise that activity by the legislator should aim at deregulation of Company Law instead of new acts and provisions. In this respect it is important to refer to the "law matters" approach again. In order to foster the development of the financial market, the legislator is well advised not to create too many legal obstacles.

First the self-regulation of the market forces has to be supported, as it has been shown with the introduction of the German Corporate Governance Code for example. The VorstOG (Management Remuneration Disclosure Act) mentioned above might have been superfluous if the Code had been worded differently. The compliance with the German Corporate Governance Code needs to receive more attention. Especially smaller stock corporations do not comply sufficiently yet[622].

Additionally, entrepreneurial risk should be accepted as an essential component of the market and not as an economy-threatening evil. Of course, it is essential that shareholders need to be protected, but this needs to happen on a basis that also leaves enough room for the stock corporations to develop.

622 Von Werder, Axel/Talaulicar, Till „Umsetzung der Empfehlungen und Anregungen des Deutschen Corporate Governance Kodex" Berlin Center of Corporate Governance, March 2006 to download at http://www.corporate-governance-code.de/ger/download/Kodex_Report_2006_Executive_Summary1.pdf at p.8

To draw a conclusion, it is important to point out positively that the legislator has tackled a number of necessary reforms in the last couple of years and therefore has improved Company Law and the environment for shareholder engagement.

10.5. Conclusion

It is essential that the mentioned solutions, financing shareholder engagement, overcoming the lack of awareness and apathy of shareholders and correcting shortcomings in Company Law will be redressed (at least to a certain extent). They are important components to make the investor an effective corporate governor. Moreover, shareholder value will also be improved, while the option of selling the shares will diminish.

Solving the financing of shareholder engagement will helps not only to improve the relationship between the shareholder and the company, but will also upvalue the corporate governance which is exercised by the general meeting.

Overcoming the lack of awareness and apathy of shareholders is needed to make them a functioning governor of the company and to avoid voting with the feet.

Shortcomings in company law need to be corrected so that some means of shareholder engagement do not run dry and that the role of the investor is fully acknowledged.

At this point it should be mentioned that corporations will not need to face an army of self-declared supervisors. The governance system existing so far should simply be put on a more effective basis and be directed into the right channels so that shareholder engagement receives the role it deserves.

Finally, if shareholder engagement is directed into the right channels it could enhance the dialogue between the corporation and its investors for the benefit of both sides.

Appendices

Figure 28: Studies Showing the Correlation between Equity Performance and Corporate Governance Activity

Study	Approach	Scope of the Study					Effect	Important Finding
		Number of Proposals	Number of Companies	Initiator/ Method	Period of the study	Observation Period of the Stock Price Performance		
Aggarwal & Williamson (2006)	new corporate governance regulations		5.200 US Firms		2001-2005	Long-term	positive and significant relation between governance and firm value – dependent on industry and size of firm	the analysis indicates that the markets already rewarded firms that had better governance
Antunovich et al. (2000)	Firm-specific differences - no specification towards corporate governance!!!			Fortune magazine: America's most admired companies	1983-1995	long-term	most admired companies had an average return of 125% in a five year period in contrast to 80% among the least admired companies	
Bebchuk, Cohen, Ferrell (2003)	24 IRRC provisions divided in to an "entrenchment" with 6 and an "other Provisions" index with 12 provisions		90 percent of all U.S. public companies	Investor Responsibility Research Center (IRRC)	1990-2003	Long-term	The higher the firm's "entrenchment" score, the lower the firm's value. No evidence on the 18 "Other provisions".	

Bizjak & Marquette (1998)	shareholder proposals	190		Data from: Investor Responsibility Research Center (IRRC)	1987-1993	stock market reaction on proposal	negative after proposal, positive (>1%) when the management restructures	shareholder proposal itself has a negative effect, as it reveals new information about the quality of the management
Carleton et al. (1998)	shareholder proposals	62	45	TIAA-CREF	1992-1996	stock market reaction on proposal	insignificant	Positive stock price reaction towards proposals to restrict anti-takeover issues and negative regarding board diversity.
Chidambaran & Woidtke (1999)	shareholder negotiation	224	168	Investigation of withdrawn proposals by In & In* in order to negotiate it	1989-1995	one year after a withdrawn proposal	positive	Shareholder negotiations should be preferred in contrast to proposals
Crutchley et al. (2000)	stock price development after CalPERS activism announcement	n.a.	47	CalPERS's target list	1992-1997	long-term	positive in the first year after the announcement (92-94), considerably negative in the following years (95-97)	shareholder activism needs to be maintained over a longer period
Del Guecio & Hawkins (1999)	shareholder proposals	266	125	5 activist funds	1987-1993	stock market reaction on proposal, 73 c. long-term	insignificant, 90-93: positive for proposals with press announcements and CalPERS involvement, negative for certain anti-takeover and board related proposals	

Drobetz, Schillhofer, Zimmermann (2003)	firm-specific corporate governance differences		91 companies in the German segments	inquiry with 91 companies	1998-2002	long-term	Outperformance of 12 % per annum	passiveness of large blockholders and institutional investors in Germany
Forjan (1999)	shareholder proposals	798	467	individuals and institutions	1978-1991	short-term	significantly negative, as shareholder proposals drain corporate resources and interrupt normal business operations	a distinguished approach on the value of shareholder activism is necessary
	shareholder negotiation	27	27	individuals and institutions	1978-1991	short-term	positive	
Gillan & Starks (2000)	shareholder proposals	763	452	individuals and institutions	1987-1994	short-term	insignificant	vote support for proposals increases over time
Gompers, Ishii & Metrick (2001)	adoption of corporate governance provisions		~1.500	Data from: Investor Responsibility Research Center (IRRC)	1990-1999	long-term	outperformance of 8.9 % per annum	a reduction of provisions and decrease in managerial power could decrease agency costs and increase shareholder wealth
Karpoff et al. (1996)	shareholder proposals	522	269	individuals and institutions	1986-1990	stock market reaction on proposal	insignificantly different from zero	no systematic evidence of policy changes among 15 firms with winning proposals

Lehmann,Warning, Weigand (2000)	performance of ownership concentrated compared to governed corporations		361 (183 listed and traded stock corporations)	Hoppenstedt Bilanzdatenbank, Bundesanzeiger, annual reports	1991-1996	long-term comparison	including families and financial institutions the performance of governed companies is significantly positive	
McKinsey & Company (2002)	investor opinion			inquiry with 200 institutional investors	2000	supposition based on inquiry	80% of the respondents would pay a premium of 18-27% (country depending) for a well governed company	
Melvin (2003)	investor focus		n.a.	Hermes Focus Fund	1998-2003	long-term	outperformance of 33.2% over five years	corporate governance structure itself is less important than the extent to which ownership oversight is exercised
Millstein & MacAvoy 1998)	Compliance with CalPERS guidelines			CalPERS		long-term	outperformance of 7% over five years	
Nesbitt (2001)	shareholder activity	n.a.	95	CalPERS	1987-2000	long-term	outperformance of 2.6% per annum	
Opler & Sokobin (1997)	shareholder negotiation	n.a.	117	Council of Institutional Investors' list	1991-1994	long-term	positive	prefer negotiation in contrast to proposals
Smith (1996)	shareholder proposals	78	51	CalPERS	1987-1993	stock market reaction on proposal to short-term	positive	Sees a significant positive stock price reaction for successful targeting events and a significant negative reaction for unsuccessful events.

Smith (1996)	shareholder negotiation	n.a.	19	CalPERS	1987-1993	stock market reaction on proposal	insignificantly different from zero	
Strickland et al. (1996)	shareholder proposals	163	85	United Shareholder Association (USA)	1990-1993	stock market reaction on proposal	insignificantly different from zero	
Strickland et al. (1996)	shareholder negotiation	53	34	USA	1992-1993	stock market reaction on proposal	Outperformance of 0.9%	
Wahal (1996)	shareholder proposals	306	146	9 activist funds	1987-1993	long-term	insignificantly different from zero	In contrast to other institutions pension funds do not appear to significantly reduce their holdings in underperforming firms in general, or in firms that they target.
Wahal (1996)	shareholder negotiation	50	n.a.	9 activist funds	1987-1993	long-term	positive	

Figure 29: Shareholder Structure of Selected Stock Corporations 2004

Source: Deutsches Aktieninstitut: DAI-Factbook August 2004 at 08.5-1, 2004
The shareholder structure is inquired by the single stock corporations at different points in time and with a different demarcation towards the single investor groups. The following charts should provide an extensive standardized overview of the shareholder structure inquiries.

2004	Total shareholders	Tied owner-ship in %	Institutional in %	Private share-holders in %	"widely held" in %	Foreign ownership in %	Employee shareholders in %	Share of employee shareholders at the capital stock in %
Aachener und Münchener Beteiligungsgesellschaft					30,2			
Aareal Bank					59,3			
Adidas Salomon AG					100,0	84,0		
AGIV Real Estate					53,0			
Aixtron					100,0			
Allianz	554.642		46,7	16,3	83,2	33,9		1,2
Altana			30,7		49,9			
Apcoa		98,3			1,7			
Augusta Beteiligungen			38,0	55,0				
Aventis						92,2		
AWD Holding					49,0			
AXA					8,3			
Axel Springer					10,6			
Baader Wertpapierhandelsbank					33,4			
Balda AG					46,8			
Bankgesellschaft Berlin					6,0			
BASF	520.000		72,0	28,0		52,4		
Bayer	495.947			24,0		39,0		
Bayerische Hypo- und Vereinsbank					81,6			
BayWa					46,2			
Beate Uhse AG					34,0			
Beiersdorf					21,7			
Beru AG			28,5	11,5		24,0		
BHW Holding AG					7,5			

2004	Total shareholders	Tied ownership in %	Institutional in %	Private shareholders in %	"widely held" in %	Foreign ownership in %	Employee shareholders in %	Share of employee shareholders at the capital stock in %
Bilfinger+Berger					75,0	25,0		
BMW			18,8		46,9			
Böwe Systec AG					39,2			
Ce Consumer Electronic	34.400		10,4		84,9			
Celesio					41,6			1,3
Centrotec					unter 42,0			
CeWe Color			25,0	35,1	60,1			
Comdirect					20,0			
Commerzbank	360.000		50,4	24,3		48,0		
Concord Effekten				20,1	43,8			
Continental					79,4			
Cybio					84,9			
DaimlerChrysler			53,0	28,0		45,0		
Degussa					49,9			
DePfa					100,0	79,2		
Deutsche Bank	503.000		65,0	9,0		53,0		
Deutsche Beteiligungs AG					49,9			
Deutsche Börse			93,0	4,0		59,0		
Deutsche EuroShop AG			19,0	60,0	79,0	2,5		
Deutsche Post					37,4			
Deutsche Telekom					57,0			
Deutsche Verkehrsbank					7,8			
Deutz					58,5			
Dialog Semiconductor					67,2			
Direkt Anlage Bank					23,6			
DIS AG			95,9	4,0	60,7			
DLogistics					70,0			
Dürr AG					23,9			
Dyckerhoff Vz.					37,8			
E.ON						43,2		

2004	Total shareholders	Tied ownership in %	Institutional in %	Private shareholders in %	"widely held" in %	Foreign ownership in %	Employee shareholders in %	Share of employee shareholders at the capital stock in %
Elmos Semiconductor					42,3			
ElringKlinger					36,4			
Epcos	114.000		51,0	24,0	75,0	29,0		
Escada				62,2				
Evotec OAI					86,0			
Fraport					29,3			
freenet.de					37,0			
Fresenius (Vz.)			85,0					
Fuchs Petrolub	9.230		37,5	37,0		31,9		
Gerry Weber					54,1			
GfK			18,6	15,1		15,2		
Grenkeleasing					47,5			
Hannover Rück	32.529		41,0	7,8	48,8	21,0		
Heidelberger Druckmaschinen					57,0			
HOCHTIEF					80,5	51,0		
Hypovereinsbank					81,6			
IDS Scheer					49,8			
IKB					50,0			
IM International Media					83,7			
Infineon					100,0			
Intershop					69,0			9,0
IWKA			18,1	48,4	100,0	33,5		
IXOS Software					12,2			
Jenoptik					84,2			
Jungheinrich	13.000		50,0	42,0		37,0		
K+S		10,0			90,0			
Karstadt-Quelle					31,2			
Klöckner-Werke					22,0			
KM Möbel					45,0			
König & Bauer			15,0				1	
Leifheit					31,9			

2004	Total shareholders	Tied owner-ship in %	Institutional in %	Private share-holders in %	"widely held" in %	Foreign ownership in %	Employee shareholders in %	Share of employee shareholders at the capital stock in %
Leoni					80,0			
Linde			48,0	20,0				
Lion Bioscience					82,4			
Loewe					64,0			
Lufthansa	440.000			43,3	91,4	23,9		
MAN			22,0					
MLP					56,6	15,7		
MPC Capital AG MVV					49,9 12,2			
Norddt. Affinerie			ca. 30,0		80,0			
Pfeiffer Vacuum Techn.					100,0	70,0		
Pfleiderer AG				ca. 10,0	86,0			
QSC AG					41,7			
Rational AG		72,3			27,7			
Repower Systems AG Rhön Klinikum AG Vz.					71,0 51,0	36,0		
SAP SI					10,0			
SGL Carbon					100,0			
Singulus Süss MicroTec					95,2 90,4			
TAKKT AG					27,5			
Teles AG					50,0			
TUI			85,0	15,0				
United Internet AG					52,0			
Villeroy & Boch Viva Media AG					91,1 38,2			
Volkswagen Vossloh			43,4	33,1	67,0			
WCM Bet.Grund.					76,6			
WEB.de		56,5			38,2			
Wella AG Vz.					56,5			
Zapf Creation					92,8			

Figure 30: Voting Results of Dax-30 AGMs 2003

company	yes	no	abstain	topic	Item no
Adidas-Salomon	7.023.456	2.514.552	79.459	Allocation of profits	2
Adidas-Salomon	9.598.506	4.832	11.347	Approval of the actions of the Members of the Board of Management	3
Adidas-Salomon	9.954.509	4.662	11.616	Approval of the actions of the Members of the Supervisory Board	4
Adidas-Salomon	9.465.509	139.574	12.304	authorisation to issue bonds, revoke the existing authorisation. Creation of conditional capital, amendment of the Articles of Association	5
Adidas-Salomon	9.582.376	23.064	11.947	authorisation to repurchase own shares	6
Adidas-Salomon	9.604.584	896	11.907	Appointment of the Auditor	7
Allianz	106.000.024	137.038	175.933	Allocation of profits	2
Allianz	105.287.015	625.186	399.866	Approval of the actions of the Members of the Board of Management	3
Allianz	105.407.386	506.594	397.629	Approval of the actions of the Members of the Supervisory Board	4
Allianz	98.833.480	7.257.962	220.532	Elections to the Supervisory Board	5
Allianz	106.013.049	144.156	154.919	Cancellation of Authorised Capital, creation of new Authorised Capital, amendment to the Articles of Association	6
Allianz	106.029.331	128.550	155.507	authorisation to acquire Company shares for trading purposes	7
Allianz	105.965.904	188.073	159.252	authorisation to acquire Company shares for other purposes	8
Allianz	105.644.936	477.554	190.671	Amendment to the Articles of Association	9
Allianz	106.019.696	110.317	183.362	Other amendments to the Articles of Association	10
Allianz	106.050.361	89.893	173.115	Approval of control and profit transfer agreements	11
Allianz	105.987.185	145.732	180.213	Cancellation of Authorised Capital, creation of new Authorised Capital, amendment to the Articles of Association	12
Altana	88.188.158	1.440	973	Allocation of profits	2
Altana	87.889.924	13.019	287.628	Approval of the actions of the Members of the Board of Management	3
Altana	17.557.670	13.019	287.565	Approval of the actions of the Members of the Supervisory Board	4
Altana	88.177.453	4.154	8.459	Elections to the Supervisory Board	5
Altana	88.179.747	2.040	8.279	Appointment of the Auditor	6
Altana	86.672.585	1.508.116	9.265	Amendments to the Articles of Association	7
Altana	88.186.978	2.386	252	Approval of profit transfer agreements	8
Altana	88.173.598	15.168	850	repurchase of shares	9
BASF	176.365.296	32.124	51.754	Allocation of profits	2
BASF	176.018.674	377.522	52.978	Approval of the actions of the Members of the Board of Management	3
BASF	176.199.678	188.904	52.745	Approval of the actions of the Members of the Supervisory Board	4
BASF	176.069.054	192.235	187.885	Appointment of the Auditor	5

company	yes	no	abstain	topic	Item no
BASF	175.433.311	312.871	702.992	election of supervisory board - single election of Mr Diederich	6
BASF	175.590.545	453.921	404.708	election of supervisory board - single election of Mr Diekmann	6
BASF	175.548.331	478.187	422.756	election of supervisory board - single election of Mr Heydebreck	6
BASF	175.793.646	307.481	348.047	election of supervisory board - single election of Mr Kelly	6
BASF	175.837.650	300.998	310.526	election of supervisory board - single election of Mr Kley	6
BASF	175.868.786	266.760	313.628	election of supervisory board - single election of Ms Köcher	6
BASF	175.853.420	282.344	313.410	election of supervisory board - single election of Mr Scholl	6
BASF	175.843.343	296.864	308.967	election of supervisory board - single election of Mr Strube	6
BASF	175.847.697	287.295	314.182	election of supervisory board - single election of Mr Studer	6
BASF	175.830.161	301.625	317.388	election of supervisory board - single election of Mr Werner	6
BASF	176.273.980	138.483	36.711	repurchase of shares	7
BASF	175.974.094	447.699	27.381	changes to articles of association	8
BASF	175.364.950	1.046.763	37.461	Approval of control and profit transfer agreements	9
Bayer	264.777.712	89.008	n.d.	Allocation of profits	2
Bayer	263.851.102	895.156	n.d.	Approval of the actions of the Members of the Board of Management	3
Bayer	264.257.111	426.224	n.d.	Approval of the actions of the Members of the Supervisory Board	4
Bayer	264.540.440	117.862	n.d.	Election to the Supervisory Board	5
Bayer	256.730.755	7.601.877	n.d.	Amendments to the Articles of Association	6
Bayer	264.664.432	216.678	n.d.	Repurchase of shares	7
Bayer	263.994.015	191.829	n.d.	Approval of a Hive-Down and Transfer Agreement	8
Bayer	263.583.378	187.406	n.d.	Approval of a Hive-Down and Transfer Agreement	9
Bayer	264.013.354	180.551	n.d.	Approval of a Hive-Down and Transfer Agreement	10
Bayer	264.288.357	144.305	n.d.	Approval of a Control and Profit Transfer Agreement	11
Bayer	264.291.326	142.139	n.d.	Approval of a Control and Profit Transfer Agreement	12
Bayer	264.300.871	127.701	n.d.	Approval of two Control and Profit Transfer Agreement	13
Bayer	264.179.799	98.642	n.d.	Appointment of the Auditor	14
Bayer	55.784	249.950.160	n.d.	Proposal to remove proposals 7-12 from the agenda	
BMW	405.479.142	3.973.735	221.760	Allocation of profits	2
BMW	408.320.097	355.918	998.879	Approval of the actions of the Board of Management	3
BMW	222.095.048	431.975	1.001.004	Approval of the actions of the Supervisory Board	4
BMW	409.316.457	104.038	254.039	Appointment of the Auditor	5
BMW	409.306.784	88.475	279.110	amendments to the Articles of Association	6
BMW	404.006.122	4.984.948	683.676	Creation of a new Authorised Capital II	7

company	yes	no	abstain	topic	Item no
Commerzbank	310.073.833	399.464	257.825	Allocation of profits	2
Commerzbank	309.786.143	712	944.267	Approval of the actions of the Board of Management	3
Commerzbank	294.159.058	16.331.191	240.873	Approval of the actions of the Supervisory Board	4
Commerzbank	309.837.604	624	892.894	Appointment of the Auditor	5
Commerzbank	307.756.668	1.631.771	1.342.393	Elections to the Supervisory Board	6
Commerzbank	310.329.670	153	401.009	Approval of a profit-and-loss transfer agreement	7
Commerzbank	310.344.027	139	386.666	Approval of a profit-and-loss transfer agreement	8
Commerzbank	289.119.905	6.212.934	15.397.993	Amendment of the Articles of Association	9
Commerzbank	310.276.859	198	453.525	authorisation to purchase its own shares for the purpose of securities trading,	10
Commerzbank	310.092.372	390	637.820	authorisation to purchase its own shares	11
Commerzbank	306.975.603	3.498.712	256.267	resolution on the conditional increase of the share capital	12
Continental	43.690.841	4.572	14.312	Allocation of profits	2
Continental	43.308.898	372.556	28.271	Approval of the actions of the Members of the Board of Management	3
Continental	43.306.358	373.211	29.836	Approval of the actions of the Members of the Supervisory Board	4
Continental	43.674.607	17.808	17.310	Appointment of the Auditor	5
Continental	43.640.289	34.292	33.644	authorisation to acquire and to dispose of own shares	6
Continental	40.441.782	3.230.789	36.844	Supervisory Board compensation	7
Continental	42.772.538	16.532	920.655	Election to the Supervisory Board	8
Continental	43.668.260	26.030	15.435	Possibility of a distribution in kind	9
Continental	43.696.633	3.536	9.556	Proxy voting rights, transmission of the Annual Shareholders´ Meeting	10
Continental	43.672.005	4.163	33.557	Other amendments to the Articles of Incorporation	11
DaimlerChrysler	386.892.294	1.121.093	6.162	Allocation of profits	2
DaimlerChrysler	385.220.227	2.167.021	16.448	Approval of the actions of the Members of the Board of Management	3
DaimlerChrysler	384.897.551	2.573.935	8.617	Approval of the actions of the Members of the Supervisory Board	4
DaimlerChrysler	385.691.791	1.721.164	10.904	Appointment of the Auditor	5
DaimlerChrysler	384.793.542	2.466.210	13.987	Repurchase of shares	6
DaimlerChrysler	384.448.405	1.900.382	9.101	Cancellation of Authorised Capital I, II and Conditional Capital II, III	7
DaimlerChrysler	383.605.355	2.567.707	6.139	Creation of a new Authorised Capital I	8
DaimlerChrysler	383.097.001	3.393.119	7.967	Creation of a new Authorised Capital II	9
DaimlerChrysler	383.294.879	3.051.187	4.803	Creation of a new Authorised Capital III	10
Deutsche Bank	203.428.606	160.810	n.d.	Allocation of profits	2
Deutsche Bank	203.724.095	932.649	n.d.	Approval of the actions of the Members of the Board of Management	3
Deutsche Bank	203.585.151	996.341	n.d.	Approval of the actions of the Members of the Supervisory Board	4

company	yes	no	abstain	topic	Item no
Deutsche Bank	202.547.190	1.529.941	n.d.	Appointment of the Auditor	5
Deutsche Bank	204.548.486	515.657	n.d.	authorisation to acquire own shares for trading purposes	6
Deutsche Bank	202.674.532	2.446.850	n.d.	authorisation to acquire own shares	7
Deutsche Bank	202.739.886	2.360.636	n.d.	Creation of new Authorised capital and amendment to the Articles of Association	8
Deutsche Bank	204.239.448	277.682	n.d.	amendments to the Articles of Association	9
Deutsche Bank	198.977.391	5.387.907	n.d.	Resolution on the adjustment of Supervisory Board remuneration	10
Deutsche Bank	200.740.302	2.923.163	n.d.	Election to the Supervisory Board	11
Deutsche Bank	204.725.950	181.650	n.d.	Approval of company agreements	12
Deutsche Börse	49.885.459	7.145	1.702	Allocation of profits	2
Deutsche Börse	49.112.899	13.361	768.046	Approval of the actions of the Members of the Board of Management	3
Deutsche Börse	49.116.367	34.328	743.481	Approval of the actions of the Members of the Supervisory Board	4
Deutsche Börse	49.264.012	457.002	173.262	Election to the Supervisory Board	5
Deutsche Börse	49.658.026	219.444	16.776	Approval of an authorised capital and changes to the articles of association	6
Deutsche Börse	49.764.377	112.437	17.462	Approval of a conditional capital, authorisation of pre-emptive rights to employees of Deutsche Börse AG	7
Deutsche Börse	47.418.706	2.457.464	17.581	Approval of a conditional capital, excluding the pre-emptive rights of the shareholders, authorisation to issue option and conversion rights	8
Deutsche Börse	49.667.842	212.285	13.954	Repurchase of shares	9
Deutsche Börse	46.439.442	3.436.992	17.247	Amendments to the Articles of Association	10
Deutsche Börse	46.438.472	3.436.522	18.687	Amendments to the Articles of Association	11
Deutsche Börse	49.873.712	11.415	9.054	Appointment of the Auditor	12
Deutsche Lufthansa	176.344.865	123.409	280.457	Allocation of profits	2
Deutsche Lufthansa	175.717.418	621.537	3.045	Approval of the actions of the Members of the Board of Management	3
Deutsche Lufthansa	173.841.112	1.500.366	5.421	Election to the Supervisory Board	5
Deutsche Lufthansa	147.488.184	28.858.088	8.458	Amendments to the Articles of Association	6
Deutsche Lufthansa	175.862.299	465.691	1.275	Repurchase of shares	7
Deutsche Lufthansa	176.101.837	163.985	895	Company Agreements	8
Deutsche Lufthansa	176.059.849	170.579	538	Appointment of the Auditor	9
Deutsche Lufthansa	170.284.491	5.965.668	n.d.	discharge of supervisory board - single discharge of Mr Schlede	4
Deutsche Lufthansa	73.516.492	102.753.154	n.d.	discharge of supervisory board - single discharge of Mr Bsirske (e)	4
Deutsche Lufthansa	170.222.533	6.028.510	n.d.	discharge of supervisory board - single discharge of Mr Breuer	4
Deutsche Lufthansa	170.258.678	5.990.568	n.d.	discharge of supervisory board - single discharge of Mr Cromme	4

company	yes	no	abstain	topic	Item no
Deutsche Lufthansa	170.280.597	5.965.021	n.d.	discharge of supervisory board - single discharge of Mr Flickenschild (e)	4
Deutsche Lufthansa	170.281.383	5.963.344	n.d.	discharge of supervisory board - single discharge of Mr Geisinger (e)	4
Deutsche Lufthansa	170.272.559	5.973.843	n.d.	discharge of supervisory board - single discharge of Mr Hartmann	4
Deutsche Lufthansa	170.261.068	5.979.978	n.d.	discharge of supervisory board - single discharge of Mr Issen (e)	4
Deutsche Lufthansa	170.161.060	6.086.865	n.d.	discharge of supervisory board - single discharge of Graf Lambsdorff	4
Deutsche Lufthansa	170.276.759	5.965.843	n.d.	discharge of supervisory board - single discharge of Mr Lieb (e)	4
Deutsche Lufthansa	170.267.490	5.976.345	n.d.	discharge of supervisory board - single discharge of Mr Macht (e)	4
Deutsche Lufthansa	170.270.769	5.971.021	n.d.	discharge of supervisory board - single discharge of Mr Neubauer	4
Deutsche Lufthansa	170.271.794	5.970.044	n.d.	discharge of supervisory board - single dischargeof Ms Ritter (e)	4
Deutsche Lufthansa	170.281.274	5.960.044	n.d.	discharge of supervisory board - single discharge of Mr Rörig (e)	4
Deutsche Lufthansa	170.270.696	5.972.721	n.d.	discharge of supervisory board - single discharge of Mr Sternberg	4
Deutsche Lufthansa	170.269.207	5.975.100	n.d.	discharge of supervisory board - single discharge of Mr Titzrath	4
Deutsche Lufthansa	170.283.048	5.961.546	n.d.	discharge of supervisory board - single discharge of Ms Windaus (e)	4
Deutsche Lufthansa	170.261.289	5.981.594	n.d.	discharge of supervisory board - single discharge of Mr Winkhaus	4
Deutsche Lufthansa	170.281.077	5.961.628	n.d.	discharge of supervisory board - single discharge of Mr Wollstadt (e)	4
Deutsche Lufthansa	170.206.953	6.037.662	n.d.	discharge of supervisory board - single discharge of Mr Zumwinkel	4
Deutsche Post	881.631.832	216.224	n.d.	Allocation of profits	2
Deutsche Post	880.871.598	880.893	n.d.	Approval of the actions of the Members of the Board of Management	3
Deutsche Post	880.851.993	915.293	n.d.	Approval of the actions of the Members of the Supervisory Board	4
Deutsche Post	881.409.036	307.764	n.d.	Appointment of the Auditor	5
Deutsche Post	880.953.351	828.344	n.d.	authorisation to purchase own shares	6
Deutsche Post	873.300.852	1.349.534	n.d.	Stock Option Plan	7
Deutsche Post	881.301.931	156.725	n.d.	Amendments to the Articles of Association	8
Deutsche Post	880.225.706	1.239.903	n.d.	amendments to the Articles of Association (SB remuneration)	9
Deutsche Telekom	2.473.173.617	15.892.870	4.451.921	Approval of the actions of the Members of the Board of Management	2
Deutsche Telekom	2.475.107.765	17.326.580	1.095.049	Approval of the actions of the Members of the Supervisory Board	3
Deutsche Telekom	2.483.893.242	4.826.733	4.739.682	Appointment of the Auditor	4
Deutsche Telekom	2.425.526.632	15.658.978	1.166.038	Elections to the Supervisory Board	5
Deutsche Telekom	2.478.678.103	13.939.951	841.288	Acquisition by company of its own shares	6
Deutsche Telekom	2.490.548.964	1.794.812	1.105.263	Profit and loss transfer agreements	7
Deutsche Telekom	2.489.961.330	2.236.901	1.235.319	Amendments to the Articles of Incorporation	8
E.ON	213.758.820	6.067	787.902	Allocation of profits	2
E.ON	214.175.151	90.513	285.125	Approval of the actions of the Members of the Board of Management	3

company	yes	no	abstain	topic	Item no
E.ON	214.106.682	100.703	285.125	Approval of the actions of the Members of the Supervisory Board	4
E.ON	214.365.071	12.556	175.151	changes to articles of association	5
E.ON	206.296.886	7.738.738	516.335	changes to articles of association	6
E.ON	213.425.058	937.538	188.863	Cancellation of Existing Conditional Capital, Creation of a new Conditional Capital and related Amendments to the Articles of Association	7
E.ON	214.401.448	37.895	111.898	Repurchase of shares	8
E.ON	206.495.985	8.000.682	91.092	Elections to the Supervisory Board	9
E.ON	212.917.294	1.362.435	270.025	Appointment of the Auditor	10
FMC	45.471.784	9.904	1.550	Allocation of profits	2
FMC	45.454.965	14.568	13.705	Approval of the actions of the Members of the Board of Management	3
FMC	45.456.794	12.871	13.627	Approval of the actions of the Members of the Supervisory Board	4
FMC	45.422.798	12.544	47.896	Appointment of the Auditor	5
FMC	45.456.066	19.612	7.560	Amendments to the Articles of Incorporation	6
Henkel	69.211.600	660	43.535	Resolution to approve the annual financial statements	1
Henkel	69.254.995	506	74	Allocation of profits	2
Henkel	69.254.093	1.258	224	Discharge of the Personally Liable Partners	3
Henkel	65.716.733	1.308	123	Discharge of the Supervisory Board	4
Henkel	60.183.138	458	124	Discharge of the Shareholders' Committee	5
Henkel	69.252.511	2.934	130	Appointment of the Auditor	6
Henkel	69.253.865	1.613	97	Approve Elections to the Supervisory Board	7
Henkel	69.254.326	1.130	119	Approve Election to the Shareholders' Committee	8
Henkel	69.253.414	2.051	110	authorisation to repurchase own shares	9
Henkel	69.253.309	220	64	Approve Amendment to the Stock Incentive Plan	10
Henkel	69.254.830	685	60	Approve Amendment to the Articles of Association	11
HVB	289.193.413	1.778.430	n.d.	Approval of the actions of the Members of the Board of Management	2
HVB	289.436.591	1.546.541	n.d.	Approval of the actions of the Members of the Supervisory Board	3
HVB	283.780.176	7.246.223	n.d.	Election of the Supervisory Board	4
HVB	276.601.960	6.249.725	n.d.	authorisation to issue bonds, option certificates or convertible certificates	5
HVB	290.405.918	308.620	n.d.	authorisation to acquire own shares for trading purposes	6
HVB	281.403.258	1.688.034	n.d.	authorisation to acquire own shares	7
HVB	290.437.200	258.179	n.d.	Amendments to the Articles of Association	8
HVB	288.901.998	478.423	n.d.	approval of spin-off plan	9
HVB	290.444.885	262.310	n.d.	approval of a control and profit and- loss transfer agreement	10

company	yes	no	abstain	topic	Item no
HVB	290.200.283	261.080	n.d.	approval of a profit and- loss transfer agreement	11
HVB	286.669.592	3.714.848	n.d.	Appointment of the Auditor	12
Infineon	227.945.589	416.001	n.d.	Approval of the actions of the Members of the Board of Management	2
Infineon	227.918.085	416.483	n.d.	Approval of the actions of the Members of the Supervisory Board	3
Infineon	228.157.635	179.954	n.d.	Appointment of the Auditor	4
Infineon	228.152.637	141.680	n.d.	approval of a profit and- loss transfer agreement	5
Linde	59.687.133	3.936	5.707	Allocation of profits	2
Linde	59.381.983	20.089	294.704	Approval of the actions of the Members of the Board of Management	3
Linde	59.375.883	22.266	298.627	Approval of the actions of the Members of the Supervisory Board	4
Linde	59.668.273	19.614	8.889	Appointment of the Auditor	5
Linde	59.642.192	33.117	21.467	Repurchase of shares	6
Linde	55.907.912	1.272.657	2.516.207	changes to articles of association	7
Linde	57.178.007	22.452	2.496.317	Elections to the Supervisory Board	8
MAN	64.478.279	710	2.755	Allocation of profits	2
MAN	64.449.323	18.617	6.985	Approval of the actions of the Members of the Board of Management	3
MAN	64.425.458	22.467	13.123	Approval of the actions of the Members of the Supervisory Board	4
MAN	63.995.894	302.706	9.828	By-Election to the Supervisory Board	5
MAN	64.263.386	20.445	7.153	Repurchase of shares	6
MAN	61.476.585	2.795.982	5.230	changes to articles of association	7
MAN	64.250.810	3.492	13.275	Other amendments to the Articles of Association	8
MAN	64.246.632	2.645	6.655	Appointment of the Auditor	9
Metro	213.441.335	683	3.168	Allocation of profits	2
Metro	250	206.551.994	6.892.827	Application of special audit	2
Metro	213.421.408	17.367	6.226	Approval of the actions of the Members of the Board of Management	3
Metro	213.380.163	19.556	45.282	Approval of the actions of the Members of the Supervisory Board	4
Metro	213.097.459	5.896	341.646	Appointment of the Auditor	5
Metro	212.579.208	289.571	576.177	Elections to the Supervisory Board	6
Metro	213.415.976	25.602	3.378	Repurchase of shares	7
Metro	213.439.567	1.796	3.593	changes to articles of association	8
Metro	213.426.915	13.040	4.930	authorisation to issue bonds; creation of conditional capital and amendment to the Articles of Association	9
Metro	213.436.724	4.774	3.388	Domination and Profit & Loss Transfer Agreement	10
Metro	213.438.018	3.480	3.388	Domination and Profit & Loss Transfer Agreement	11

company	yes	no	abstain	topic	Item no
Metro	213.436.445	3.430	3.088	Domination and Profit & Loss Transfer Agreement	12
MLP	46.232.501	451.504	n.d.	Approval of the actions of the Members of the Board of Management	2
MLP	27.057.951	311.477	n.d.	Approval of the actions of the Members of the Supervisory Board	3
MLP	61.804.857	362.868	n.d.	Appointment of the Auditor	4
MLP	62.031.879	258.246	n.d.	Elections to the Supervisory Board	5
MLP	62.009.480	273.786	n.d.	Amendments to the Articles of Association	6
Munich Re	97.737.601	4.967.553	8.840	Allocation of profits	2
Munich Re	102.181.890	100.499	431.897	Approval of the actions of the Members of the Board of Management	3
Munich Re	102.180.695	101.103	432.322	Approval of the actions of the Members of the Supervisory Board	4
Munich Re	102.416.246	256.931	40.923	Elections to the Supervisory Board	5
Munich Re	102.621.423	71.179	16.177	Repurchase of shares	6
Munich Re	99.463.283	3.224.045	26.140	Cancel the existing Conditional Capital, grant a new Authorisation to issue Warrants; create a new Conditional Capital and amend the Articles of Association	7
Munich Re	95.951.285	2.546.212	4.216.154	Cancel the existing Authorisation to issue Bonds, approve a new Authorisation to issue Bonds; create a new Conditional Capital and amendment to the Articles of Association	8
Munich Re	97.670.362	5.021.552	22.305	other amendments to the articles of association	9
Munich Re	102.679.970	13.376	19.983	Approve the conclusion of various Intercompany Agreements	10
RWE	325.897.351	15.047	n.d.	Allocation of profits	2
RWE	315.840.311	10.016.156	n.d.	Approval of the actions of the Members of the Board of Management	3
RWE	313.022.670	12.838.760	n.d.	Approval of the actions of the Members of the Supervisory Board	4
RWE	325.785.995	35.364	n.d.	Appointment of the Auditor	5
RWE	305.399.896	19.106.452	n.d.	Elections to the Supervisory Board	6
RWE	310.134.554	15.723.203	n.d.	changes to the articles of association	7
RWE	325.863.132	24.690	n.d.	Approval of an Intercompany Agreement	8
RWE	325.862.925	20.215	n.d.	Approval of an Intercompany Agreement	9
SAP	180.132.196	11.012	41.809	Allocation of profits	2
SAP	142.847.577	33.051	62.818	Approval of the actions of the Members of the Board of Management	3
SAP	108.060.477	43.692	61.564	Approval of the actions of the Members of the Supervisory Board	4
SAP	180.078.679	16.984	88.791	Appointment of the Auditor	5
SAP	180.037.335	67.034	81.557	Elections to the Supervisory Board	6
SAP	180.032.269	14.585	138.950	changes to the articles of association	7
SAP	179.921.030	45.632	46.205	Repurchase of shares	8

company	yes	no	abstain	topic	Item no
SAP	179.834.061	54.462	125.761	authorisation to use equity derivatives in connection with the acquisition of treasury shares	9
Schering	67.746.225	580.152	70.479	Allocation of profits	2
Schering	66.993.519	1.299.391	103.947	Approval of the actions of the Members of the Board of Management	3
Schering	67056321	1299336	41200	Approval of the actions of the Members of the Supervisory Board	4
Schering	67.716.968	592.599	87.290	Appointment of the Auditor	5
Schering	67.789.045	582.406	25.406	Repurchase of shares	6
Schering	67.803.488	585.496	7.873	changes to the articles of association	7
Siemens	367.632.490	273.626	1.343.899	Allocation of profits	2
Siemens	366.483.131	1.046.400	1.739.537	Approval of the actions of the Members of the Board of Management	3
Siemens	310.216.103	785.318	1.772.621	Approval of the actions of the Members of the Supervisory Board	4
Siemens	366.589.751	1.102.744	1.554.972	Appointment of the Auditor	5
Siemens	366.412.567	1.292.075	1.532.952	Repurchase of shares	6
Siemens	366.002.777	1.574.392	1.653.136	Elections to the Supervisory Board	7
Siemens	367.381.749	245.987	1.607.914	changes to the articles of association	8
Siemens	367.471.908	278.333	1.491.449	changes to the articles of association	9
Siemens	308.673.377	2.318.412	1.789.687	changes to the articles of association	10
Siemens	366.082.327	1.443.167	1.709.075	Creation of an authorised capital and amendents to the articles of association	11
Siemens	365.899.898	1.543.800	1.774.806	Authorisation to issue bonds, create a Conditional Capital, amendments to the Articles of Association	12
ThyssenKrupp	316.273.893	53.308	n.d.	Allocation of profits	2
ThyssenKrupp	315.866.935	98.683	n.d.	Approval of the actions of the Members of the Board of Management	3
ThyssenKrupp	315.847.465	126.035	n.d.	Approval of the actions of the Members of the Supervisory Board	4
ThyssenKrupp	316.170.154	114.557	n.d.	Appointment of the Auditor	5
ThyssenKrupp	316.261.587	50.617	n.d.	changes to the articles of association	6
ThyssenKrupp	315.868.439	463.247	n.d.	changes to the articles of association	7
ThyssenKrupp	316.261.610	48.955	n.d.	Approve the conclusion of various Intercompany Agreements	8
ThyssenKrupp	316.252.951	66.292	n.d.	Repurchase of shares	9
TUI	96.229.495	38.953	11.540	Allocation of profits	2
TUI	96.148.427	124.871	6.880	Approval of the actions of the Members of the Board of Management	3
TUI	96.123.777	148.276	6.625	Approval of the actions of the Members of the Supervisory Board	4
TUI	96.171.938	85.663	22.577	Elections to the Supervisory Board	5
TUI	94.269.365	1.996.171	14.642	Appointment of the Auditor	6

company	yes	no	abstain	topic	Item no
TUI	96.204.687	54.727	19.428	Cancellation of existing Conditional Capital, creation of a new Conditional Capital and related Amendments to the Articles of Association	7
TUI	96.206.678	57.555	14.559	Repurchase of shares	8
TUI	96.174.966	90.049	12.877	changes to the articles of association	9
TUI	96.175.247	91.866	11.709	changes to the articles of association	10
TUI	96.186.743	70.760	21.339	changes to the articles of association	11
TUI	96.242.529	20.412	15.901	changes to the articles of association	12
TUI	96.244.189	20.301	14.352	changes to the articles of association	13
TUI	96237304	25921	15617	Approval of an Intercompany Agreement	14
Volkswagen	95.870.570	4.388.994	n.d.	Allocation of profits	2
Volkswagen	100.003.843	538.593	n.d.	Approval of the actions of the Members of the Board of Management	3
Volkswagen	100.002.269	540.130	n.d.	Approval of the actions of the Members of the Supervisory Board	4
Volkswagen	99.920.485	553.107	n.d.	changes to the articles of association	5
Volkswagen	99.913.739	576.414	n.d.	Repurchase of shares	6
Volkswagen	99.948.866	519.930	n.d.	Approve the conclusion of various Intercompany Agreements	7
Volkswagen	99.961.959	558.655	n.d.	Appointment of the Auditor	8

Figure 31: Resolution Quorums outside the General Meeting

Right to	1% of the capital stock or an interest of 100.000	5% of the capital stock or an interest of 500.000	5% of the capital stock	10% of the capital stock or an interest of 1.000.000 €	10% of the capital stock
Determine items on the agenda (§122 s.2 AktG)		X			
File an alternative claim in the shareholders own name (§ 147a s.1 AktG)	X				
Action to set aside a resolution, with which distributable net retained profit is given to the shareholders, resulting in the impossibility to pay shareholders a dividend of at least 4% of the share capital less any contributions not yet called in (§ 254 s.2.s.3 AktG)		X			
Apply at court for a special audit, because of suspecting inadmissible undervaluation in the financial statements (§ 258 s2 s.3 AktG)	X				
Apply at court for decision not to accept final ascertainment in a § 258 AktG-procedure (§ 260 s.1 s.1 AktG) and if necessary raise an appeal in this procedure (§ 260 s.3 s.4 AktG)		X			
Apply at court to appoint or remove liquidators if important grounds therefore exist (§ 265 s.3 s.1 AktG)		X			
Apply at court to appoint special auditors if (excluding the rules in § 315 s.1) other facts support the suspicion that the company has suffered an undue disadvantage(§ 315 s.2 AktG)		X			
Call in a general meeting (§ 122 s.1 s.1 AktG)			X		
Call in a general meeting in the case of a take-over (§ 62 s.2 s.1 UmwG)			X		
Apply at court to remove a member of the supervisory board for material cause (§ 103 s.3 s.3 AktG)				X	
Apply at court to appoint special auditors, if the general meeting has rejected the appointment of such (§ 142 s.2 s.1 AktG)	X				
Apply at court to appoint another special auditor if the general meeting has appointed one (§ 142 s.4 s.1 AktG)				X	
Apply at court to appoint special representatives to assert alternative claim (§ 147 s.2 s.2 AktG)				X	
Apply at court to appoint another then the elected auditor (§ 318 s.3 s.1 HGB)				X	
Shareholders who are entitled take part in the vote on a separate resolution can request a separate meeting or notice of a proposal to be voted on separately (§ 138 s.3 AktG)					X
Block the liberating group settlement of the parent company, if the shareholders of the subsidiary company have applied for settlement and progress report 6 months before the end of the business year (§ 291 s.3 s.1 HGB)					X
Necessity to approve a liberating group settlement, when the minority shareholder own less					X

than 10 % of the shares (§ 291 s.3 s.2 HGB)					
Demand a merger resolution of the corporation, which is taking over (§ 62 s.1 UmwG)					X

Figure 32: Resolution Quorums in the General Meeting

	Simple majority	Qualified majority	Simple majority and additional requirement	Simple majority (variable <>75%)	Simple majority (variable >75%)	Unanimity
Change of the articles of association to adjust a new legal composition of the supervisory board (§ 97 s.2 s.4 AktG)	X					
Election of members of the supervisory board (§ 101 s.1 and 3 AktG)	X					
Removal of members of the supervisory board if the requirements necessary for the right to appoint are no longer met (§ 103 s.2 AktG)	X					
Reduction of the remuneration of members of the supervisory board (§ 113 s.1 s.4 AktG)	X					
Ratification of the acts of members of the management and supervisory board (§ 120 s.1 s.1 AktG)	X					
Appointment of special auditors (§ 142 s.1 s.1 AktG)	X					
Assert a claim for damages to the company (§ 147 s.1 s.1 AktG – according to §§ 46-48, 53, 93, 116, 117 AktG	X					
Appropriation of Profits (§ 174 s.1 AktG)	X					
Capital reduction by redemption of shares in the case of § 237 s.3 AktG (§ 237 s.4 AktG)	X					
Removal of elected members of the supervisory board – 75% (§ 103 s.1 s.2 AktG)		X				
Replacement of the rejected approval of management responsibilities through the general meeting – 75% (§ 111 s.4 s.5 AktG)		X				
Adoption of rules of procedure for the general meeting and its later annulment or alteration – 75% (§ 129 s.1 AktG)			X			
Upholding of multiple voting rights shares – 75% (§ 5 s.1 EGAktG)			X			
Waive and settlement of claims for damages against the incorporators - record an objection in the minutes 10% (§ 50 s.1 AktG)			X			
Waive and settlement of claims for damages against the management board - record an objection in the minutes 10% (§ 93 s.4 s.3 AktG)			X			
Duty of care and responsibility of members of the supervisory board (§ 93 AktG applies analogously) - record an objection in the minutes 10% (§ 116 AktG)			X			

Liability for damages - Use of the influence over the corporation (§ 93 AktG applies analogously) - record an objection in the minutes 10% (§ 117 AktG)			X			
Alteration of the articles of association – no alteration of the company object (§ 179 s.2 AktG)				X		
Capital increase with shareholder subscription rights (§ 182 s.1 AktG)				X		
Capital increase out of corporate capital (§ 182 s.1 in conjunction with § 207 AktG)				X		
Decision to give out convertible or adjustment bonds, respectively the corresponding decision to authorise (§ 221 s.1 AktG)				X		
Cure of post formation obligatory contracts(§ 52 s.5 AktG)					X	
Alteration of the company object (§ 179 s.2 AktG)					X	
Transfer of the complete company assets (§ 179a AktG)					X	
Capital increase (including subscription right) with preference shares without voting right (§ 182 s.1 s.2 AktG)					X	
Capital increase with at least partial exclusion of shareholder subscription rights (§ 186 s.3 AktG, also in conjunction with § 203 s.1 or § 221 s.4 AktG)					X	
Decision to increase the capital qualified (§ 193 s.1 AktG)					X	
Decision over the authorisation to increase the capital (approved capital) (§ 202 s.2 AktG)					X	
Capital decrease (§ 222 s.1 AktG, also in conjunction with § 237, sometimes § 229 AktG)					X	
Decision to close down the company (§ 262 s.1 No.2 AktG)					X	
Decision to continue the closed down company (§ 274 s.1 AktG)					X	
Cure of nullity, as far as it is based on the company object (§ 276 in conjunction with § 179 s.2 AktG)					X	
Approval of company contracts of any kind of the subsidiary company and of control and shifting of profit contracts of the parent company (§ 293 s.1 and 2 AktG), same is valid for the reference in § 295 s.1 AktG to alter a company contract					X	
Integration of a 100% subsidiary company (§319 s.2 AktG)					X	
Integration of a (95%) majority subsidiary company (§ 320 in conjunction with § 319 s.2 AktG)					X	
Decision to merge (§ 65 s.1, if necessary in conjunction with § 73 UmwG)					X	
Decision to division, respectively assignment of the assets (§ 125 in conjunction with § 176 respectively § 176 in conjunction with § 65 UmwG)					X	

Form alteration into a limited partnership (§ 233 s.2 UmwG)					X	
Form alteration into a limited company/limited partnership on shares (in the latter case is approval of every shareholder necessary)(§ 240 s.1 UmwG)					X	
Form alteration into a cooperative without duty to subsequent payment (§ 252 s.2 UmwG)					X	
Imposition of collateral obligations (§ 180 I AktG)						X
Restriction of transferability of registered shares or interim certificates (§ 180 II AktG)						X
Renunciation of report and audit with company contracts, mergers and other, is only valid with public record and notarial certified approval (§ 293 a s.3 AktG and § 8 s.3 UmwG including a number of references on this)						X
Conversion into an unlimited private company (OHG or BGB-company)(§ 233 s.1 UmwG)						X
Conversion into corporative with duty to subsequent payment (§ 252 s.1 UmwG)						X
Conversion into a limited company, if the shareholder is unable to keep his interest in the company (§ 242 UmwG)						X

§ 23 s.5 AktG states that the articles of association can determine their own majority of votes:

§ 133 s.1 AktG – Articles of association can determine majority of votes if the law does not give any specific regulations

Majority of votes and no opening clause – compelling:

§ 103 s.2 s.2 AktG – removal of members of the supervisory board

§ 113 s.1 s.4 AktG – remuneration of members of the supervisory board

§ 142 s.1 s.1 AktG – appointment of special auditors

Only vaster majorities and tightened additional requirements

numerous e.g. § 202 s.2 s.3 AktG – conditions for authorised capital

Other majorities and other requirements

numerous e.g. § 103 s.1 s.3 AktG – removal of members of the supervisory board

Special regulations:

Majority, which is necessary for the preparing respectively curing decision:

§ 83 s.1 AktG - preparation of decisions by the general meeting

§ 242 AktG - approved decision of contestable decisions of the general meeting

Figure 33: Petition Right with Different Types of Shares

	Qualified majority of votes- 75%	Simple majority of votes in gm (variable >75%)	Simple majority of votes (variable <>75%)
Special meeting of shareholders with preference shares (§ 141 s.3 s.2 and 3 AktG)	X		
Complete or partial exclusion of the subscription right (§ 141 s.3 AktG)	X		
Disadvantage for certain type of shares with an alteration of the articles of association (reference to the majority in the general meeting + 75% majority (statute dispositive))(§ 179 s.3 AktG)	X		
Special decision (simple majority): capital increase – approval of the different type of shares (must be eligible to vote)(§ 182 s.2 AktG)		X	
Special decision (simple majority): creation of conditional capital (§ 193 s.1 AktG)		X	
Special decision (simple majority): approved capital (§ 202 s.2 AktG)		X	
Special decision (simple majority): convertible or adjustment bonds (§ 221 s.1 AktG)			X
Decrease of Capital (simplified, regular, norm) (§§ 222 s.2, 229, 237 AktG)		X	
Special decision (simple majority): merger (§ 65 s.2 UmwG (if necessary in conjunction with § 73 UmwG) and division and transfer of property (§§ 125 and 176 UmwG)		X	
Outside shareholders (company contract necessary): Alteration of adjustment and compensation payments (§ 295 s.2 in conjunction with § 293 s.1 s.2 and3 AktG)		X	
Outside shareholders (company contract necessary): Annulment of the contract (§ 296 in conjunction with § 293 s.1 s.2 and3 AktG)		X	
Outside shareholders (company contract necessary): Notice of the contract by the management of the subsidiary company (§ 297 s.2 in conjunction with § 293 s.1 s.2 and3 AktG)		X	

The mentioned majorities are also valid for the limited partnership on shares (§ 278 s.3 AktG).

Exceptions are:

-Notice, approval of the closing down and the petition to close down by order of the court (§ 289 s.4 AktG)

-Differing voting rights of the personal liable partner (§§ 285 s.1, 285 s.2, 286 s.1 AktG)

Definitions

American Depository Receipt[623] **- A**merican Depositary Receipts (ADRs) are one of the most popular methods by which US investors gain exposure to foreign securities (For ADRs to be within the US pricing levels, they may represent more than one share of a foreign Issuer or a fraction of one share of a foreign Issuer). In comparison to owning foreign securities directly, ADRs provide benefits to US investors who wish to own foreign securities, including easy transfer of shares, payment of dividends in US dollars, and facilitation of compliance with foreign investment restrictions and requirements. Similarly, ADRs and other forms of depositary receipts also are attractive vehicles for many non-US investors for investments in emerging markets. Non-US investors of ADRs appreciate the greater security and liquidity that these instruments offer over direct investment in certain markets.

ADRs, which are negotiable certificates Issued by a US bank or trust company, represent ownership interests in shares of a foreign Issuer that have been deposited with a depositary. The deposited securities are usually held by a custodian in the country of the foreign Issuer.

ADRs may be established either as "sponsored" or "unsponsored" programs. Unsponsored ADRs are typically private arrangements among investors, broker-dealers, and a depositary bank, without the participation of the Issuer. Sponsored ADRs are established jointly between an Issuer and a depositary under the terms of a depositary agreement that sets out the rights and responsibilities of the Issuer, depositary, and ADR holder. Because ADRs must be sponsored to be listed on a national exchange or on NASDAQ, this paper focuses on sponsored ADRs.

Different Types of ADRs

There generally are three different types of sponsored ADR programs – Level I, Level II, and Level III, each with its own set of legal and regulatory requirements.1 Generally, the higher level ADRs indicate a higher level of Issuer involvement with the ADR program and a greater amount of information made available by the Issuer to the public. Both ADRs and the deposited securities must be registered under the Securities Act of 1933 (Securities Act) if there is a public offering of securities in ADR form.1 Deposited securities must be registered under the Securities Act of 1933 if a foreign Issuer or its affiliate is selling securities to the public in the United States. Registration of deposited securities, however, would not be required when neither the Issuer nor an affiliate is engaged in a public offering of the deposited securities.

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623 Definition by the International Corporate Governance Network at www.icgn.org

Level I ADRs are used when an Issuer does not wish to, or is not allowed to, list its securities on a national securities exchange; Level I ADRs are traded in the "pink sheets." Level I ADRs must be registered with the SEC although most Level I Issuers seek exemption from SEC reporting requirements.

Level II ADRs can be listed and traded on national securities exchanges and must comply with the full registration and reporting requirements of the Securities Act and the Securities Exchange Act of 1934 (Exchange Act), which include initial registration on Form F-6, registration statements on Form 20-F, and annual reports and interim financial statements. Level II ADRs also require compliance with other selected securities laws, including Section 13 reporting of stock transactions. Because a Level II ADR does not involve a public offering in the United States of the shares underlying the ADRs, the underlying shares do not have to be registered under the Securities Act.

Level III ADRs are the highest profile programs under which Issuers float a public offering of depositary receipts in the United States and list the receipts on a national securities exchange. Level III receipts are subject to the same registration and reporting requirements as Level II receipts with the additional requirement that a Form F-1 registration statement for the securities underlying the ADRs also must be filed with the SEC. The Form F-1 includes a prospectus to inform potential investors about the company and the risks associated with the offering.

Under SEC rules for Level II and III ADRs, the depositary bank must make copies of shareholder communications, proxies, and reports received from the Issuer available for inspection by the ADR holders.1 In their initial registration, foreign Issuers are required to disclose the terms of the deposit, including corporate governance rights of Level II and III ADR holders.1 For example, foreign Issuers must disclose provisions, if any, with respect to the procedure for voting the deposited securities and the transmission of notices, reports, and proxy soliciting materials. For Level II and III ADRs, foreign Issuers also are required to disclose in their SEC registration filings any provisions of foreign law or governing documents of the Issuer that would limit the rights of nonresident or foreign owners of ADRs to hold or vote the securities or to receive dividends, interest, and other payments.

Antigreenmail[624] – Greenmail refers to the agreement between a large shareholder and a company in which the shareholder agrees to sell his stock back to the company, usually at a premium, in exchange for the promise not to seek control of the company for a specified period of time. Antigreenmail provisions prevent such arrangements unless the same repurchase offer is made to all shareholders or the transaction is approved by shareholders through a vote. They are thought to discourage

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624 All the following definitions are taken from GOMPERS, Paul A./ISHII, Joy L./METRICK, Andrew "Corporate Governance and Equity Prices" July 2001 at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=278920 p.37-42

accumulation of large blocks of stock because one source of exit for the stake is closed, but the net effect on shareholder wealth is unclear (Shleifer and Vishny (1986a)). Five states have specific antigreenmail laws, and two other states have "recapture of profits" laws, which enable firms to recapture raiders' profits earned in the secondary market. We consider recapture of profits laws to be a version of antigreenmail laws (albeit a stronger one). The antigreenmail category includes both firms with the provision and those incorporated in states with either antigreenmail or recapture of profits laws.

Blank check preferred stock – This is preferred stock over which the board of directors has broad authority to determine voting, dividend, conversion, and other rights. While it can be used to enable a company to meet changing financial needs, it can also be used to implement poison pills or to prevent takeover by placement of this stock with friendly investors. Companies who have this type of preferred stock but who have required shareholder approval before it can be used as a takeover defence are *not* coded as having this provision in our data.

Business Combination laws – These laws impose a moratorium on certain kinds of transactions (e.g., asset sales, mergers) between a large shareholder and the firm for a period usually ranging between three and five years after the shareholder's stake passes a pre-specified (minority) threshold.

Bylaw and **Charter** amendment limitations – These provisions limit shareholders' ability to amend the governing documents of the corporation. This might take the form of a supermajority vote requirement for charter or bylaw amendments, total elimination of the ability of shareholders to amend the bylaws, or the ability of directors beyond the provisions of state law to amend the bylaws without shareholder approval.

Classified board – A classified board is one in which the directors are placed into different classes and serve overlapping terms. Since only part of the board can be replaced each year, an outsider who gains control of a corporation may have to wait a few years before being able to gain control of the board. This provision may also deter proxy contests, since fewer seats on the board are open each year.

Compensation plans with changes in control provisions – These plans allow participants in incentive bonus plans to cash out options or accelerate the payout of bonuses should there be a change in control. The details may be a written part of the compensation agreement, or discretion may be given to the compensation committee.
Director indemnification **contracts** – These are contracts between the company and particular officers and directors indemnifying them from certain legal expenses and judgments resulting from lawsuits pertaining to their conduct. Some firms have both

"indemnification" in their bylaw/charter and these additional indemnification "contracts".

Control-share cash-out laws enable shareholders to sell their stakes to a "controlling" shareholder at a price based on the highest price of recently acquired shares. This works something like fair-price provisions (see below) extended to non-takeover situations.

Cumulative voting – Cumulative voting allows a shareholder to allocate his total votes in any manner desired, where the total number of votes is the product of the number of shares owned and the number of directors to be elected. By enabling them to concentrate their votes, this practice helps enable minority shareholders to elect favoured directors. Cumulative voting and secret ballot (see below), are the only two provisions whose presence is coded as an *increase* in shareholder rights, with an additional point to G if the provision is absent.

Directors' duties allow directors to consider constituencies other than shareholders when considering a merger. These constituencies may include, for example, employees, host communities, or suppliers. This provision provides boards of directors with a legal basis for rejecting a takeover that would have been beneficial to shareholders. 31 states also have laws with language allowing an expansion of directors' duties, but in only two of these states (Indiana and Pennsylvania) are the laws explicit that the claims of shareholders should not be held above those of other stakeholders [Pinnell (2000)]. We treat firms in these two states as though they had an expanded directors' duty provision unless the firm has explicitly opted out of coverage under the law.

Fair-Price Requirements – These provisions limit the range of prices a bidder can pay in two-tier offers. They typically require a bidder to pay to all shareholders the highest price paid to any during a specified period of time before the commencement of a tender offer and do not apply if the deal is approved by the board of directors or a supermajority of the target's shareholders. The goal of this provision is to prevent pressure on the target's shareholders to tender their shares in the front end of a two-tiered tender offer, and they have the result of making such an acquisition more expensive. This category includes both the firms with this provision and the firms incorporated in states with a fair price law.

Golden parachutes – These are severance agreements which provide cash and non-cash compensation to senior executives upon a triggering event such as termination, demotion, or resignation following a change in control. They do not require shareholder approval.

Director **indemnification** – This provision uses the bylaws and/or charter to indemnify officers and directors from certain legal expenses and judgments resulting from lawsuits pertaining to their conduct. Some firms have both this "indemnification" in their bylaws/charter and additional indemnification "contracts". The cost of such protection can be used as a market measure of the quality of corporate governance [Core (2000)].

Limitations on director **liability** – These charter amendments limit directors' personal liability to the extent allowed by state law. They often eliminate personal liability for breaches of the duty of care, but not for breaches of the duty of loyalty or for acts of intentional misconduct or knowing violation of the law.

Pension parachute – This provision prevents an acquirer from using surplus cash in the pension fund of the target in order to finance an acquisition. Surplus funds are required to remain the property of the pension fund and to be used for plan participants' benefits.

Poison pills – These securities provide their holders with special rights in the case of a triggering event such as a hostile takeover bid. If a deal is approved by the board of directors, the poison pill can be revoked, but if the deal is not approved and the bidder proceeds, the pill is triggered. In this case, typical poison pills give the holders of the target's stock other than the bidder the right to purchase stock in the target or the bidder's company at a steep discount, making the target unattractive or diluting the acquirer's voting power. The early adopters of poison pills also called them "shareholder rights" plans, ostensibly since they give current shareholders the "rights" to buy additional shares, but more likely as an attempt to influence public perceptions. A raider-shareholder might disagree with this nomenclature.

Secret ballot – Under secret ballot (also called confidential voting), either an independent third party or employees sworn to secrecy are used to count proxy votes, and the management usually agrees not to look at individual proxy cards. This can help eliminate potential conflicts of interest for fiduciaries voting shares on behalf of others, or can reduce pressure by management on shareholder-employees or shareholder-partners. Cumulative voting (see above) and secret ballot, are the only two provisions whose presence is coded as an *increase* in shareholder rights, with an additional point to *G* if the provision is absent.

Executive **severance** agreements – These agreements assure high-level executives of their positions or some compensation and are not contingent upon a change in control (unlike Goldenor Silver parachutes).

Silver parachutes – These are similar to golden parachutes in that they provide severance payments upon a change in corporate control, but unlike golden parachutes, a large number of a firm's employees are eligible for these benefits.

Special meeting requirements – These provisions either increase the level of shareholder support required to call a special meeting beyond that specified by state law or eliminate the ability to call one entirely.

Supermajority requirements for approval of mergers – These charter provisions establish voting requirements for mergers or other business combinations that are higher than the threshold requirements of state law. They are typically 66.7, 75, or 85 percent, and often exceed attendance at the annual meeting. This category includes both the firms with this provision and the firms incorporated in states with a "control-share acquisition" law. These laws require a majority of disinterested shareholders to vote on whether a newly qualifying large shareholder has voting rights. In practice, such laws work much like supermajority requirements.

Unequal voting rights – These provisions limit the voting rights of some shareholders and expand those of others. Under time-phased voting, shareholders who have held the stock for a given period of time are given more votes per share than recent purchasers. Another variety is the substantial-shareholder provision, which limits the voting power of shareholders who have exceeded a certain threshold of ownership.

Limitations on action by **written consent** – These limitations can take the form of the establishment of majority thresholds beyond the level of state law, the requirement of unanimous consent, or the elimination of the right to take action by written consent.

List of Abbreviations

Acts

AktG – Aktiengesetz (Stock Corporation Act)

HGB – Handelsgesetzbuch (Trading Act)

BGB – Bürgerliches Gesetzbuch (Civil Code)

InvG – Investmentgesetz (Investment Act)

WpÜG – Wertpapiererwerbs- und Übernahmegesetz (Security Acquisition and Takeover Act)

KStG - Körperschaftssteuergesetz (Corporation Tax Act)

WpHG - Wertpapierhandelsgesetz (Securities Trade Act)

SpruchG - Spruchverfahrensgesetz (Judgement Procedure Act)

KapMuG – Kapitalanleger-Musterverfahrensgesetz (Act for Master Actions by Investors)

KontraG - Gesetz zur Kontrolle und Transparenz im Unternehmensbereich (Corporation Control and Transparency Act)

NaStraG - Gesetz zur Namensaktie und zur Erleichterung der Stimmrechtsausübung (Law on Registered Shares and Simplified Rules for the Exercise of Voting Rights)

TransPuG - Transparenz- und Publizitätsgesetz (Transparency and Publicity Act)

UMAG – Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (Act for Enterprise Integrity and the Modernisation of the Right to Appeal)

VorstOG - Vorstandsvergütungs-Offenlegungsgesetz (Management Remuneration Disclosure Act)

Institutions

BGH Bundesgerichtshof (Federal High Court)

EU – European Union

NIRI - American National Investor Relations Institute

BVI – Bundesverband Investment und Asset Management (Association of German Institutional Investors)

AFG – Association Francaise de la Gestion (Association of French Institutional Investors)

DSW Deutsche Schutzvereinigung für Wertpapierbesitz (German Association to Protect Shareholding)

OLG – Oberlandesgericht (Higher Regional Court)

LG – Landgericht (District Court)

Other

CEO – Chief Executive Officer

IPO – Initial Public Offering

AGM – Annual General Meeting

SRI – Social Responsible Investment

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