

**Swiss Investment Foundation  
for Sustainable Development**



**Corporate Governance:  
A Challenge  
for Swiss Companies**

October 2003



ethos.

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## SUMMARY

Following major failures observed in the management of several listed companies over the last few years, investors have become more vigilant regarding the principles of corporate governance applied by the companies in which they invest. With a view to protecting the investors' interests and regaining their confidence, the Swiss stock exchange issued the "SWX Directive on Information Relating to Corporate Governance" in 2002. This Directive specifies the information that companies must henceforth disclose in their annual reports regarding corporate governance.

As an institutional investor, the ethos Investment Foundation pays particular attention to the level of compliance with the new SWX Directive, as well as the general application of principles of best practice in corporate governance. In pursuance of this objective, ethos has carried out a study on the standards of corporate governance achieved by the 100 major companies listed on the Swiss stock exchange which held their annual general meetings before 30 September 2003.

The study analysed and rated the 100 companies according to their levels of compliance with:

- The SWX Directive disclosure requirements.
- Principles of best practice in corporate governance.

The results revealed that 37 companies (5 of which are listed on the SMI index) lack transparency in matters relating to corporate governance. The ethos Foundation is therefore unable to classify them as being in compliance with the requirements of the SWX Directive.

With regard to the principles of best practice in corporate governance, companies were classified according to the ethos "Corporate Governance" rating taking into account their levels of transparency and disclosure of information, capital structure, the composition and organisation of the board of directors, the independence of the auditors, and shareholders' participation rights.

The leaders in corporate governance are the companies that comply equally with the Directive requirements concerning transparency, and with principles of best practice in corporate governance. In this respect, UBS, Swiss Re, CS Group, Unaxis and Zurich Financial Services lead the way. At the other end of the scale, Zehnder, Conzzeta, Belimo, Ems-Chemie and Edipresse lag far behind.

Since the study aims to contribute to an improvement in corporate governance in Switzerland, it also includes a list of proposals for clarifying the "SWX Directive on Information Relating to Corporate Governance" and The "Code of best practice for Corporate Governance" issued by *economiesuisse*.

## INTRODUCTION

The majority of stock exchange markets have adopted codes of best practice in corporate governance in order to protect investors and regain the confidence they lost following a series of cases of corporate governance failures.

Since 2002, Switzerland also benefits from two major documents designed to improve corporate governance within companies listed on the Swiss Exchange. The first set of rules is to be found in the "Swiss Code of Best Practice for Corporate Governance", published by *economiesuisse* (the Federation of Swiss enterprises), which sets out recommendations for public companies. The second document, issued by the Swiss stock exchange, is the "SWX Directive on Information Relating to Corporate Governance". The latter sets out what information relating to corporate governance must henceforth be provided in a company's annual report.

In its capacity as an institutional investor, the ethos Foundation pays particular attention to the level of compliance with the new Directive as well as measures relating to best practice in corporate governance adopted by the companies of which ethos is a shareholder. In pursuance of this objective, ethos carried out a detailed study on corporate governance within 100 major companies listed on the Swiss Exchange, which held their Annual General Meetings before 30 September 2003.

This study is divided into four sections. The **first section** sheds light on the companies' level of disclosure in corporate governance by analysing the manner in which they comply with the requirements of the SWX-Directive. The **second section** goes on to analyse the same companies' overall compliance with best practice in corporate governance. For this purpose, ethos established a set of principles based on the leading international codes of best practice in corporate governance. The **third section** brings together the results obtained in the preceding sections, i.e. the level of disclosure required by at the Swiss Stock Exchange and the level of compliance with codes of best practice in corporate governance. Finally, the **fourth section** sets out proposals to clarify the SWX-Directive and complement the *economiesuisse* code in order to enable companies to better meet the expectations of their shareholders in matters of corporate governance.

Through this study, ethos aims to provide investors with data concerning the corporate governance of the major companies listed on the Swiss Exchange. In addition, it aims to encourage these companies to further improve their levels of best practice in corporate governance.

# 1. TRANSPARENCY: THE SWX-DIRECTIVE

## 1.1 INTRODUCTION TO THE SWX-DIRECTIVE

The Swiss exchange took a significant step towards greater disclosure in corporate governance when it issued the “SWX-Directive on Information Relating to Corporate Governance” in July 2002. This new Directive provides a genuine incentive for companies to improve their corporate governance by encouraging greater transparency, the cornerstone of best practice. This requirement constitutes an incentive for numerous companies by providing them with a means to reassure their shareholders concerning their managerial and control mechanisms.

In practice, the SWX-Directive requires companies to disclose information on corporate governance in their annual reports. Disclosure must pertain to all areas of corporate governance, divided into the following nine sections and covering 68 items :

- 1) Group structure and shareholders (5 items)
- 2) Capital structure (12 items)
- 3) Board of directors (14 items)
- 4) Management board (5 items)
- 5) Compensations, shareholdings and loans (16 items)
- 6) Shareholders' participation rights (8 items)
- 7) Change-in-control and defence measures (2 items)
- 8) Auditors (5 items)
- 9) Information policy (1 question)

Only section 5, concerning Compensations, is mandatory. The others are subject to the principle of “comply or explain”, which implies that if a company withholds certain information it must provide reasons for each case of non-disclosure.

## 1.2 SWISS COMPANIES AND THE SWX-DIRECTIVE: RESULTS

### 1.2.1 General observations

The SWX-Directive includes two types of questions. The first is dealt with through itemised information or references to statutory provisions. The second is more descriptive in nature and relates to the companies' operational structure, control instruments or the internal organisation of governing bodies. With regard to the second category, the SWX-Directive leaves a certain leeway concerning the details to be disclosed. As a result, companies' disclosure varies considerably in quality.

Furthermore, some companies refer the reader to documents other than the annual report. The Swiss Exchange authorises this practice but nevertheless specifies that excessive reference to other documents may lead to loss of clarity. It further specifies that all cited sources should be easily accessible (i.e. immediately and free of charge), which is far from being the case.

It is important to note that not all items apply to all companies. For instance, item 6.1.1 refers to voting rights' restrictions. In such cases, the SWX-Directive advises companies to indicate that the relevant item is not applicable, advice that several companies failed to follow. Some of the

companies merely insert a statement at the beginning of the corporate governance section indicating that all omissions correspond to non-applicable items.

Finally, it appears that all companies failed to apply the “comply or explain” principle (applicable to all sections except section 5 on compensations, which is mandatory). In fact, not a single company provided any explanation for its refusal to disclose information on certain items.

### **1.2.2 Overall results**

The 100 major companies listed on the Swiss Exchange which held their Annual General Meetings (AGMs) before 30 September 2003 ([Annex 1](#)), were analysed with regard to Compliance to the SWXDirective.

Companies have been classified according to their level of disclosure vis à vis the SWXDirective. The level of disclosure reflects the quality of the company’s response to the 68 items covered by SWX-Directive. Items are weighted according to their respective significance and the detailed information required for each. A rating of 100 points corresponds to perfect disclosure in matters covered by SWX-Directive. Further details concerning methodology are provided in [Annex 2](#).

The ethos Foundation considers that a company should obtain at least 80 points to achieve a satisfactory level of disclosure as required by the SWX-Directive. Nevertheless, a company cannot be considered to have achieved compliance with the SWX-Directive if it fails to disclose all information required under each item of section 5 (compensations), i.e. the section where answers are mandatory.

As can be observed in [table 1](#), 71 companies obtained at least 80 points and therefore pass the disclosure test. In order to obtain the exact number of companies in full compliance with the SWX-Directive, it is necessary to deduct the 8 companies that obtained 80 points but failed to disclose all information relevant to items in section 5. There are, therefore, 63 companies that achieved compliance. Swiss Re and UBS achieved the highest level of compliance.

A total of 37 companies (5 of which are on the SMI index) cannot be considered by the ethos Foundation to have complied with the SWXDirective.

**Table 1 : Level of transparency and compliance with SWX-Directive**

Satisfactory level of transparency			
Rank	Name		Points
1	SWISS RE	SMI	98.0
2	UBS	SMI	98.0
3	HIESTAND		97.7
4	ZURICH FIN SERV	SMI	97.7
5	SIG		97.3
6	BANK SARASIN		96.7
7	CS GROUP	SMI	96.7
8	ZUGER KB		96.7
9	BANK COOP		96.3
10	SAURER		95.0
11	CLARIANT	SMI	94.3
12	UNAXIS	SMI	94.3
13	NESTLE	SMI	94.0
14	PSP		94.0
15	SIA ABRASIVES		94.0
16	JULIUS BAER	SMI	93.7
17	KUONI		93.0
18	SWISSCOM	SMI	93.0
19	ADECCO	SMI	92.7
20	FORBO		92.7
21	SCHINDLER		92.7
22	GEORG FISCHER		92.3
23	SERONO	SMI	92.3
24	VP BANK		92.0
25	CHARLES VOEGELE		91.7
26	BEKB / BCBE	**	91.3
27	BALOISE	SMI	91.0
28	BERNA BIOTECH		91.0
29	RIETER		91.0
30	NOVARTIS	SMI	90.7
31	HOLCIM	SMI	90.3
32	SIEGFRIED		90.3
33	JELMOLI		90.0
34	KOMAX		90.0
35	SULZER	SMI	90.0
36	GEBERIT		89.7
37	INFICON		89.7
38	VALORA	**	89.7
39	KUDELSKI	SMI	89.3
40	TAMEDIA		89.3
41	ACTELION		89.0
42	LUZERNER KB		88.7
43	VALIANT		88.7
44	DAETWYLER		88.0
45	LINDT & SPRUENGLI		87.7
46	BASLER KB		87.0
47	SAIA-BURGESS		87.0
48	SWISS LIFE	SMI **	87.0
49	SYNTHESES-STRATEC		86.7
50	ABB	SMI	86.3
51	SARNA KUNSTSTOFF	**	86.3
52	MICRONAS		85.7
53	TECAN		85.7
54	AFFICHAGE		84.7
55	SYNGENTA	SMI	84.7
56	RICHEMONT	SMI	84.3
57	LIECHTENSTEIN LBK		84.0
58	SWISS PRIME SITE	**	84.0
59	SWISSLOG		84.0
60	REG REAL ESTATE	**	83.7
61	LOGITECH		83.3
62	PHONAK		83.3
63	PHOENIX MECANO		83.0
64	PARGESA		83.0
65	CIBA SPECIALITES	SMI **	82.7
66	ZSCHOKKE		82.3
67	NATIONALE SUISSE		82.0
68	MOEVENPICK	**	82.0
69	ST GALLER KB		81.0
70	LONZA	SMI	80.7
71	GIVAUDAN	SMI	80.0

Insufficient level of transparency			
Rank	Name		Points
72	GURIT-HEBERLEIN	**	79.3
73	KUEHNE & NAGEL	**	79.3
74	VONTOBEL		79.3
75	ROCHE	SMI	79.0
76	SIKA		79.0
77	PUBLIGROUPE		78.7
78	BASELLAND KB	**	78.3
79	SWATCH	SMI **	77.7
80	ZUEBLIN IMMOB		77.7
81	GALENICA		77.3
82	HELVETIA PATRIA		77.3
83	SEZ	**	77.0
84	NOBEL BIOCARE		76.7
85	SWISSFIRST	**	76.0
86	LEICA GEOSYSTEMS	**	75.7
87	BON APPETIT	**	72.7
88	SGS	SMI **	72.7
89	ALLREAL	**	71.7
90	EDIPRESSE		71.7
91	STRAUMANN	**	70.3
92	BOBST		69.7
93	OZ	**	68.7
94	BUCHER		68.3
95	CONVERIUM	**	68.3
96	BELIMO	**	67.7
97	EMS-CHEMIE		67.3
98	BACHEM		66.3
99	ZEHNDER	**	64.7
100	CONZZETA	**	61.7

**\*\*** Companies that failed to provide information concerning items in section 5 (compensations) which is mandatory.

### **1.2.3 Detailed results**

In the sections below, the numbering of items corresponds exactly to those in the Annex of the SWX-Directive.

#### ***Section 1: Group structure and shareholders***

This section covers questions relating to the group's operational structure, the identity of significant shareholders or groups of shareholders as well as cross-shareholdings exceeding 5% of total voting rights or capital.

Generally speaking, compliance to the SWXDirective requirements is satisfactory. Item 1.1.1, concerning operational structure, was the only item in this section that was not always clearly addressed in detail (in 19% of cases, disclosure was incomplete or withheld).

#### ***Section 2: Capital structure***

This section deals with questions relating to the company's capital : total share capital, type of shares issued, details concerning authorised and conditional capital and changes in shareholders' equity within the last three financial years. It also covers issues pertaining to the transfer of shares, admissibility of nominee registrations, as well as outstanding convertible bonds and options.

Broadly speaking, compliance with the requirements of the SWX-Directive was satisfactory, with the two following exceptions:

- Changes in shareholders' equity (item 2.3) : 53% of companies gave incomplete information or failed to disclose information altogether. According to the SWXDirective, companies must disclose all information not only concerning share capital, but also reserves and net income, for the last three financial years. In several cases, companies disclosed changes of share capital but not of reserves or net income. In some cases, the companies disclosed shareholder equity changes for only the last two financial years.
- Restrictions on transferability and nominee registration (items 2.6.1 and 2.6.4) : 30% of companies that apply restrictions did not disclose their procedures for waiving them. In some cases, the explanation was provided in connection with voting rights restrictions (items 6.1.1 and 6.1.3) or statutory quorums (item 6.2). A number of companies refer the reader to their articles of association.

#### ***Section 3: The Board of Directors***

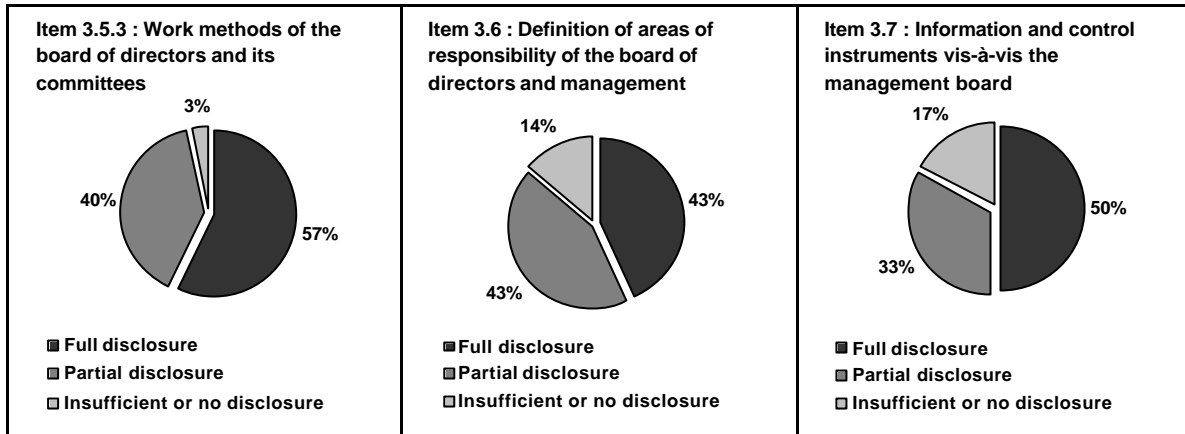
This section deals with two types of questions:

- Information concerning individual members of the board of directors.
- The organisational structure, activities and functioning of the board of directors.

Overall compliance with the requirements of the SWXDirective is satisfactory with regard to information on individual members of the board. Nevertheless, 21% of companies partially or entirely failed to disclose details relating to their board members' professional and educational background. However, comparison with disclosure issued prior to the Directive's entry into force reveals a marked improvement in the investors' access to information relating to the exact composition of the board of directors.

In contrast, disclosure pertaining to the organisation and functioning of the board of directors (items 3.5.3, 3.6 and 3.7) is far from complete.





#### **Section 4: Management Board**

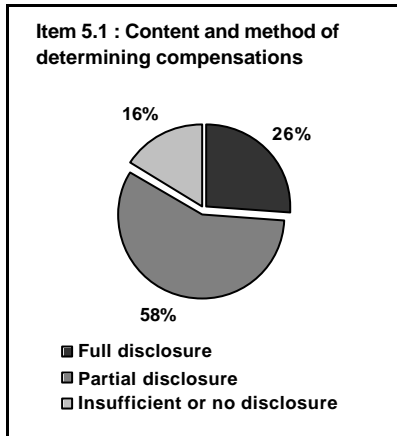
Section 4 deals with questions related to information concerning individual members of the management board, as well as management contracts between the company and other companies not belonging to the group.

In general, compliance with the requirements of the SWX Directive is satisfactory. However, 23% of companies disclosed incomplete information or entirely failed to disclose information concerning the board members' professional and educational background.

#### **Section 5: Compensations, shareholdings and loans**

Section 5 is the only section where disclosure is mandatory, while the principle of "comply and explain" applies to all other sections.

The first question (5.1) deals with compensation policies in general. Answers should provide information relevant to the philosophy of compensation policy as well as the principles regarding the responsibility and procedures for the establishment of remuneration. In general, the quality of information disclosed is insufficient and does not enable investors to form a clear picture of remuneration policies. In cases where information was provided, most companies disclosed the identity of those responsible for the establishment of remunerations and the elements of remuneration (salary, bonuses, and shareholding programmes). However, there were several missing elements, in particular regarding the ratio of fixed to variable remuneration, performance criteria, maximum individual awards, peer groups for comparisons.



The other questions in this section concern data relating to the various elements of remuneration paid to directors and members of the management board (e.g. the total cash remuneration of the management board, the number of shares and options allotted to board directors and the management board). The majority of companies complied with the requirements of the SWX-Directive. In fact, some companies exceeded the level of disclosure required by the Directive by providing information concerning remuneration of individual board members (Novartis, Convergium, Micronas, Nobel Biocare, Swissfirst, Zurich Financial Services).

However, with regard to item 5.9 relative to the highest total compensation paid to a director, 10 companies did not disclose the relevant figure (Belimo, Banque Cantonale Bernoise BEKB-BCBE, Bon Appetit, Gürit-Haberlein, Leica, Mövenpick, Real Estate Group, Société Générale de Surveillance, Zehnder). By contrast, 27 companies showed greater transparency than required by disclosing the identity of the recipient of the highest total compensation.

Given that responses to question 5.9 are mandatory, the ethos Foundation considers those companies that did not respond correctly to this section as non-compliant with the SWX-Directive, which should entail a sanction by the stock exchange.

### **Section 6: Shareholders' participation rights**

This section covers issues regarding voting-rights restrictions, statutory quorums, rules governing the convocation of general shareholders' meetings, rules for adding items to the agenda of the general shareholders' meetings and rules for registering shareholders in the issuers' share register.

The quality and clarity of disclosure varied considerably. The following are the areas where disclosure was most deficient:

- Conditions and deadlines for adding an item to the agenda: 27% provided incomplete information (they disclosed the minimum amount but not the deadline) and 6% provided no information.
- Deadline for registering in the issuers' share register in order to participate in general shareholders' meetings: 19% provided incomplete information or withheld information altogether.
- Procedures and conditions for waiving statutory voting-rights restrictions: 17% provided incomplete information or withheld information altogether.

### **Section 7: Change-in-control and defence measures**

This section requires that statutory clauses on “opting out” and “opting up” be disclosed. Furthermore, clauses concerning change-in-control agreements and plans in favor of members of the board of directors and/or management board should also be disclosed.

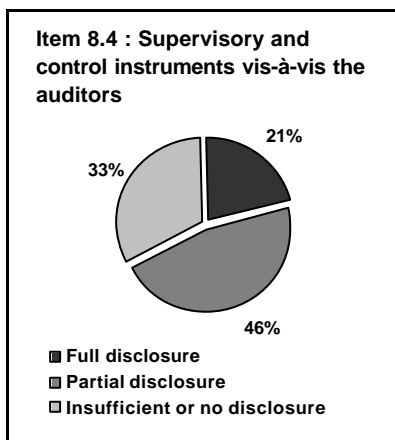
In general, disclosure of information relevant to this section showed a high level of compliance with the SWX Directive.

### **Section 8: Auditors**

This section includes questions related to the duration of the mandate of the external auditor, fees paid for auditing the company’s accounts and for any additional services, as well as information relating to the supervisory and control instruments vis à vis the auditors.

Disclosure concerning the beginning of the mandate of the audit firm and of the lead auditor is generally satisfactory, as is data concerning the auditor’s fees. Several companies (Adecco, Banque Coop, Givaudan, Kudelski, Logitech, Novartis, Roche) voluntarily disclosed an itemised list of specific honorariums disbursed for services other than auditing.

However, the description of supervisory and control instruments vis à vis the auditors (question 8.4) is thoroughly insufficient despite its extreme relevance to the investors. More specifically, companies often restrict themselves to disclosing that the audit committee is responsible for supervising the auditors but fail to disclose details concerning the methods of control of the external auditors, frequency of contacts between the board and auditors, etc.



### **Section 9: Information policy**

This section consists of just one question concerning the information policy. Only half the companies under review answered fully by indicating the frequency and type of information disclosed, the permanent sources of information and contact addresses available to shareholders.

## 2. BEST PRACTICE: THE ETHOS “CORPORATE GOVERNANCE” RATING

### 2.1. INTRODUCTION TO THE ETHOS RATING

The concept of corporate governance may be defined as the rules that govern the roles and balance of power between a company's various stakeholders, for instance, its shareholders, board of directors, management board, and auditors. Over the years, the majority of stock exchange markets have adopted codes of best practice in corporate governance in order to encourage companies to adopt best practice, and to reassure investors.

For long-term investors, the standards or corporate governance of companies of which they are shareholders are of primary importance. These rules mainly deal with transparency in the disclosure of information, protection of shareholder rights, guarantees concerning the equal treatment of shareholders, the independence of the board of directors, the alignment of the shareholders' and directors' interests regarding remuneration, and independence in methods of control and auditing procedures.

In this respect, “The Code of best practice for Corporate Governance”, published in 2002 by *economiesuisse* represented, for a majority of Swiss companies, an important step towards a better awareness of principles of good governance. In particular, it is the first time that recommendations concerning shareholder rights and the composition and responsibilities of the board of directors were formulated for the benefit of companies. Nevertheless, this document is merely a first step in the right direction. Section 4.2 provides insight into the ethos Foundation's proposals for enhancing the *economiesuisse* code.

In order to assess the current level regarding corporate governance achieved by Swiss companies, ethos has established a “Corporate Governance” rating. The rating provides a detailed analysis of the following subjects :

- 1) Transparency
- 2) Capital structure
- 3) The board of directors
- 4) The external auditors
- 5) Shareholders' participation rights.

### 2.2 SWISS COMPANIES AND THEIR ETHOS RATING: RESULTS

#### 2.2.1 Overall results

The ethos “Corporate Governance” rating was applied to the same 100 companies analysed above for compliance with the SWX-Directive ([Annex 1](#)).

Each company was assessed in detail in five subjects : transparency, capital structure, the board of directors, the auditors, and shareholders' participation rights. Each subject is weighted according to its significance to the investor. In [table 2](#), the ethos rating is expressed in percentage points, the highest rating being 100%. Further details concerning methodology are provided in [Annex 3](#).

**Table 2 : ethos' "Corporate Governance" rating**

Ethos "Corporate Governance" rating			Ethos "Corporate Governance" rating		
Rank	Name	Score	Rank	Name	Score
1	UBS	SMI 92.7%	51	SERONO	SMI 61.7%
2	SWISS RE	SMI 85.7%	52	NOBEL BIOCARE	61.3%
3	CS GROUP	SMI 84.7%	53	GALENICA	61.0%
4	LOGITECH	83.7%	54	SIA ABRASIVES	61.0%
5	UNAXIS	SMI 83.7%	55	BOBST	60.3%
6	CHARLES VOEGELE	81.3%	56	SIEGFRIED	60.3%
7	HOLCIM	SMI 81.3%	57	VALORA	60.0%
8	ZURICH FIN SERV	SMI 81.3%	58	ZSCHOKKE	60.0%
9	CONVERIUM	80.7%	59	KOMAX	59.7%
10	NOVARTIS	SMI 79.7%	60	ZUEBLIN IMMOB	59.0%
11	SIG	79.3%	61	ACTELION	58.7%
12	SYNGENTA	SMI 79.3%	62	HELVETIA PATRIA	58.0%
13	ST GALLER KB	77.3%	63	HIESTAND	58.0%
14	LEICA GEOSYSTEMS	77.0%	64	KUEHNE & NAGEL	57.7%
15	LONZA	SMI 76.7%	65	OZ	57.7%
16	BEKB / BCBE	76.3%	66	FORBO	57.3%
17	GIVAUDAN	SMI 76.3%	67	PHOENIX MECANO	57.3%
18	SWISS LIFE	SMI 76.3%	68	BUCHER	57.0%
19	CIBA SPECIALITES	SMI 75.7%	69	JULIUS BAER	SMI 56.0%
20	NESTLE	SMI 75.7%	70	VONTOBEL	56.0%
21	SWISS PRIME SITE	75.3%	71	PUBLIGROUPE	55.3%
22	SULZER	SMI 74.0%	72	SWISSFIRST	55.3%
23	SAURER	73.7%	73	BANK COOP	54.7%
24	ZUGER KB	73.3%	74	NATIONALE SUISSE	54.7%
25	TAMEDIA	72.3%	75	BANK SARASIN	53.3%
26	BALOISE	SMI 72.0%	76	BERNA BIOTECH	53.0%
27	SAIA-BURGESS	71.3%	77	PARGESA	53.0%
28	TECAN	71.3%	78	SGS	SMI 50.7%
29	VALIANT	70.7%	79	SWATCH	SMI 49.3%
30	GEBERIT	70.0%	80	SIKA	49.0%
31	RIETER	69.7%	81	BACHEM	48.7%
32	INFICON	69.3%	82	REG REAL ESTATE	48.0%
33	GEORG FISCHER	68.0%	83	SEZ	47.0%
34	LUZERNER KB	68.0%	84	RICHEMONT	SMI 46.7%
35	MICRONAS	67.3%	85	MOEVENPICK	46.3%
36	PSP	67.0%	86	ALLREAL	46.0%
37	STRAUMANN	67.0%	87	KUDELSKI	SMI 45.7%
38	SWISSCOM	SMI 67.0%	88	EDIPRESSE	43.0%
39	ADECCO	SMI 66.7%	89	LINDT & SPRUENGLI	42.0%
40	ABB	SMI 65.3%	90	EMS-CHEMIE	41.7%
41	VP BANK	65.0%	91	CONZZETA	41.3%
42	AFFICHAGE	64.3%	92	BON APPETIT	41.0%
43	PHONAK	64.3%	93	BELIMO	40.7%
44	SWISSLOG	64.0%	94	DAETWYLER	40.7%
45	KUONI	63.7%	95	BASLER KB	39.0%
46	LIECHTENSTEIN LBK	63.7%	96	BASELLAND KB	37.7%
47	SYNTHES-STRATEC	63.7%	97	GURIT-HEBERLEIN	37.7%
48	SARNA KUNSTSTOFF	63.0%	98	JELMOLI	37.7%
49	CLARIANT	SMI 62.7%	99	SCHINDLER	32.7%
50	ROCHE	SMI 61.7%	100	ZEHNDER	26.3%

## 2.2.2 Detailed results

### Item 1: Information

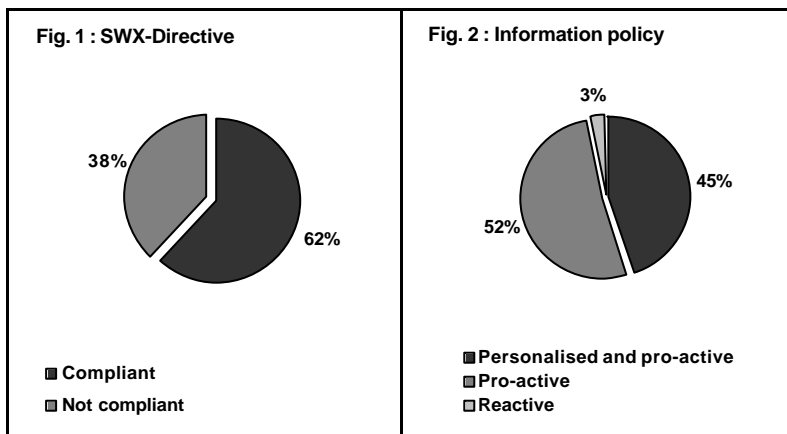
Transparency and the disclosure of information are fundamental to good corporate governance. They are an indispensable condition for shareholder confidence. The principle of transparency should be applied to corporate governance rules, as well as to financial data, and social and environmental information.

The SWX-Directive guidelines for corporate governance have undeniably improved standards of transparency of companies listed on the Swiss Exchange. At the same time, the growth of the Internet has greatly enhanced companies' ability to facilitate the distribution of information.

In its evaluation, ethos takes into consideration:

- The level of transparency and compliance with the SWX-Directive.
- The manner in which significant information is disclosed (pro-active or reactive: for instance, possibilities of subscribing to automatic distribution lists for press releases and documents etc.).

### Results



There is room for tangible improvement in the levels of transparency achieved by a number of Swiss companies. In particular, 38% of companies are not in compliance with “SWX-Directive on Information Relating to Corporate Governance”. Only 45% of companies offer investors the possibility of subscribing to a mailing list in order to obtain significant information on a regular basis.

### Item 2: Capital structure

Capital structure is a key element of corporate governance. Certain fundamental shareholder rights, such as voting rights, depend on capital structure, which therefore has a direct impact on the exercise of power within the company and on methods of control.

One of the most important aspects of holding shares is the right to vote in proportion of one's participation in the company's share capital, which corresponds to the “one share, one vote” principle. However, in Switzerland, public companies have various legal mechanisms that enable them to disconnect voting rights than capital from an investor's share of the capital. An investor

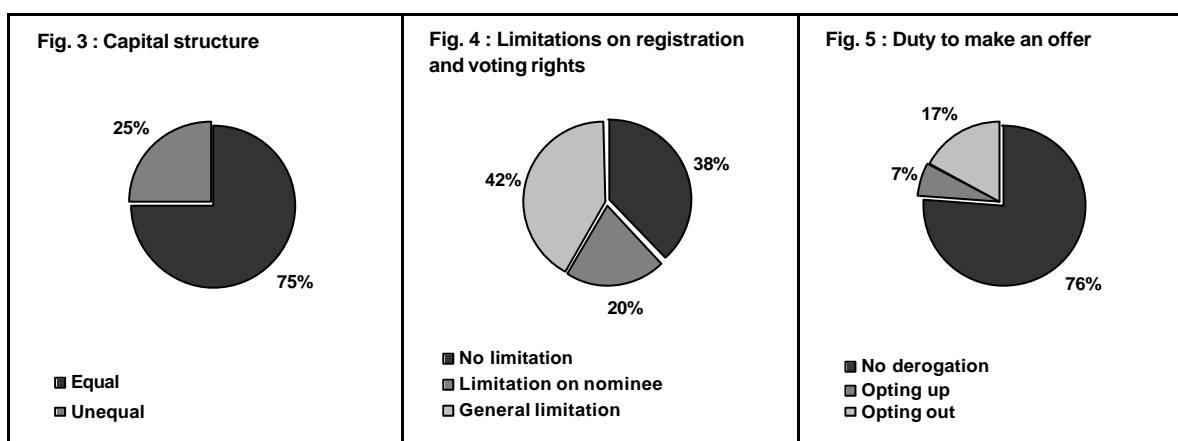
can therefore have more or less, or no voting rights at all in companies with participation certificates, restrictions on transferability and nominee registrations, restrictions on shareholder registration or voting rights or preferential voting rights. Although it is important to view unequal capital structures in the light of a company's history, ethos considers that such structures should not be encouraged or reinforced.

Swiss law requires investors who acquire more than 33,3% of voting rights of a company to make an offer to acquire all the shares of the company. However, Swiss law authorises a company to derogate from this duty if they introduce a provision in the articles of association ("opting out" clause). Companies can also introduce clauses in their articles of association whereby they raise the threshold for compulsory offering from 33% to 49% of the voting rights ("opting up" clause). Clauses allowing to derogate from the duty to make an offer run counter to minority shareholders' interests since they allow for unequal treatment of investors.

Ethos took the following points into consideration when carrying out its evaluation:

- Capital structure.
- Restrictions on registration in the share register, nominee registrations and voting rights restrictions.
- Derogations from the duty to make an offer (opting out and opting up clauses).

## Results



The equal treatment of shareholders remains a sensitive issue for several companies :

- 25% of companies still have unequal capital structures, and consequently, do not apply the principle of "one share, one vote".
- Only 38% of companies have no restrictions on the registration of shareholders and on shareholder voting rights.
- 25% of companies have introduced opting-out or opting-up clauses in their articles of association. This enables a potential buyer to derogate from the duty to make an offer to all shareholders if he exceeds the 33.3%, or respectively 49% threshold of the capital.

### **Item 3: The Board of Directors**

Shareholders should not interfere with the operational management of a company. However, it is their duty to elect the members of the board of directors who will in turn be responsible for

directing and supervising the company's affairs at the highest level (art. 716a CO). The composition and organisation of the board are therefore of vital importance to the long-term investor.

It is in the shareholders' interest to reaffirm their confidence in the board of directors on a regular basis. For this reason, the duration of a director's mandate should be as short as possible, in general a year. Needless to say, a candidate may be re-elected to a new term of office. When mandates exceed a year, the mandates of specific directors should be staggered. In this way, it is possible to ensure that the board is gradually renewed without having to elect most or all its members at once.

Given the complexity and diversity of the board of directors' functions, its size is also very important. The board must consist of enough members to provide a variety of competencies and to ensure an optimal composition of its key committees. It must also include a sufficient number of independent members. On the other hand, too many members would hinder the board of directors' efficiency by creating a group of directors who would feel less involved in decision-making. Listed companies should therefore have boards consisting of 9 to 15 members.

In order to fulfil its mandate in an objective and independent manner, the board of directors must include a number of independent members. Following the example set in the new version of the British "Combined Code" published in July 2003, the ethos Foundation considers that at least half the board members should be independent. The role of independent members is extremely important since their presence ensures that the board committees function effectively. A board of directors must include three key committees, i.e. the audit committee, the nomination committee, and the remuneration committee. Each committee should in principle consist of at least three members, who should generally be independent non-executive directors.

In order to meet ethos' requirements for independence, a director should:

- a. Not hold (or have held) an executive position in the company.
- b. Not be or represent a significant stakeholder (shareholder, supplier, client, government, employees).
- c. Not be or represent a consultant, business or financial partner of the company.
- d. Not be related to a significant shareholder or executive member of the company.
- e. Not hold a cross-directorship.
- f. Not receive any additional substantial remuneration from the company.
- g. Not have served on the board of directors for more than 10 years.

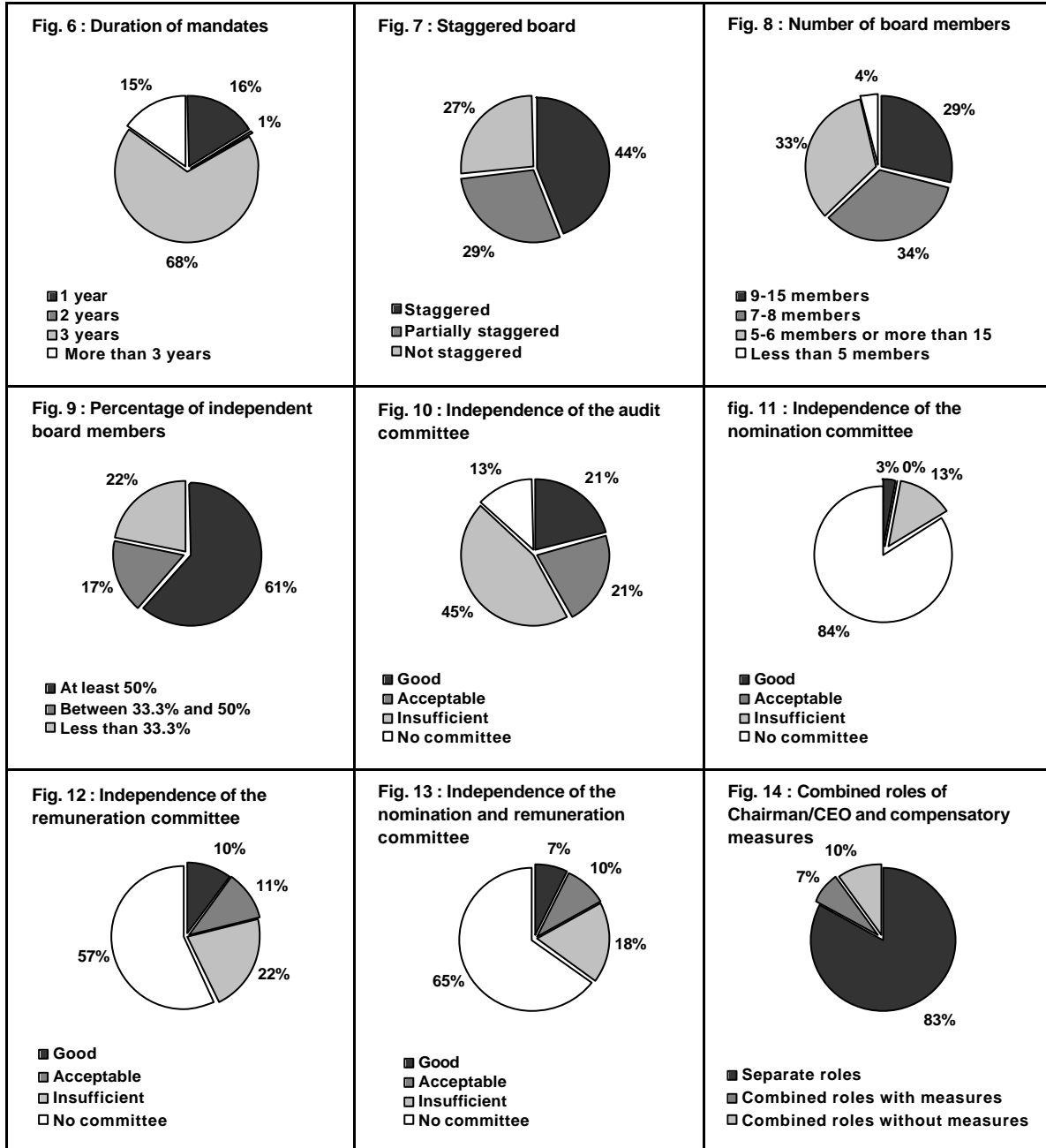
As a general principle, the positions of Chairman of the board of directors and CEO should not be held by the same person. If, for specific reasons, these two functions are assumed by a single person, measures should be taken to counterbalance this concentration of power. In particular, it is advisable to appoint a lead director who can convene board meetings in the absence of the Chairman-CEO. Moreover, the Chairman-CEO should not serve on the board's three key committees.

In evaluating the board of directors, ethos takes the following points into consideration:

- The duration of the director's mandates and whether they are staggered.
- The size of the board of directors.
- The existence of key committees and their independence.
- The independence of the board of directors.
- The joint or separate functions of the Chairman of the board and the CEO, as well as the existence of adequate compensatory measures.



## Results



**Table 3 : Combined Chairman/CEO positions**

Company	Lead Director	More than 50% independents on the board	Key committees in place and Chairman/CEO not in committees
ABB	yes	yes	yes
Ciba	yes	yes	no
Dätwyler	no	no	no
Edipresse	no	no	no
EMS-Chemie	no	no	no
Galenica	yes	no	yes
Kudelski	yes	no	no
Lindt&Sprüngli	no	no	no
Novartis	yes	yes	no
Pargesa	no	no	no
Richemont*	no	no	no
Roche	no	no	no
Schindler	no	no	no
SEZ	no	yes	no
Synthes-Stratec	no	yes	no
Zehnder	no	no	no
Züblin	no	no	no

\*as from October 2003

The composition and organisation of boards of directors vary considerably in terms of quality and compliance with international standards of best practice.

- The overall level of independence of most boards of directors is satisfactory. Nevertheless, it is debatable whether independent directors adequately fulfil their role since they are often a minority on the three key board committees (audit committee, nomination committee, and remuneration committee).
- Over the years, the size of boards of directors has been greatly reduced. Over one-third of the boards consist now of 6 or less members, making it difficult to create independent and competent committees.
- With regard to audit committees, there is clearly room for improvement since 13% of the companies have not yet created one. Moreover in 45% of cases, the audit committees' level of independence is insufficient.
- There has been a reduction in the number of companies that permit a single person to assume the joint function of Chairman of the board of directors and CEO. Nevertheless, this structure persists in 17 companies, 10 of which have not adopted compensatory measures to counteract this concentration of powers.

#### **Item 4: Auditors**

Given the importance for shareholders of monitoring the integrity of accounts, it is essential that the auditing body be strictly independent of the company whose accounts are to be audited. When electing the external auditor, shareholders should be assured of the auditor's independence. Since the SWX-directive's entry into force, shareholders have had access to

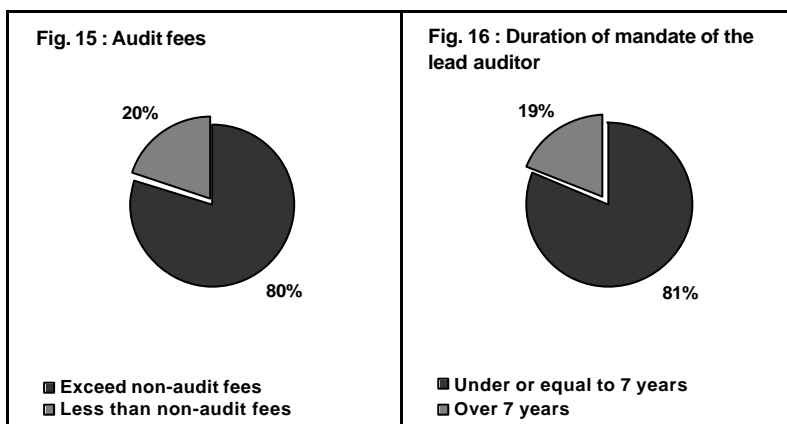
useful information. In particular, companies must now provide for the separate disclosure of the total of auditing honorariums, and additional honorariums received by auditors for other services. Ethos considers that if additional honorariums repeatedly exceed auditing honorariums, then the auditors' independence can be called into question.

Another element that could compromise the auditors' independence is the duration of their mandate. The *Chambre fiduciaire suisse* specifies that a lead auditor, responsible for an auditing mandate in a listed company, should not hold office for a period exceeding 7 years. This principle shall enter into force as of 2004.

In evaluating the auditors, ethos took the following points into consideration:

- The total of auditing honorariums vis à vis additional honorariums for other services.
- The number of years since the lead auditor's assumption of his mandate.

## Results



In 20% of the companies analysed, additional honorariums received by the auditors for services other than auditing exceeded the auditing honorariums. Best practice requires that, in future, companies entrust non-auditing mandates to other consultants so as to ensure the auditors' independence.

### **Item 5: Shareholders' participation rights**

In order to evaluate best practice in corporate governance, it is also necessary to assess how easily shareholders can exercise their rights.

A particularly important right is the right to put items on the agenda of general meetings. In Switzerland, this right is reserved to significant shareholders. Article 699, al 3, CO specifies that one or more shareholders must hold shares for a minimum of CHF1 million in par value, unless the company's articles of association provide for a lower figure. This threshold is not negligible since it often corresponds to several million francs in market value. In order to ensure that this right remains accessible to average shareholders, companies are encouraged to make statutory provisions for a lower threshold, particularly if the par value of shares has been reduced to less than CHF 10.

The presentation of the agenda of general meetings is extremely important since shareholders must, in full knowledge of the facts, make decisions on each item put to the vote. Among the subjects which are often presented in insufficient detail, ethos can mention information

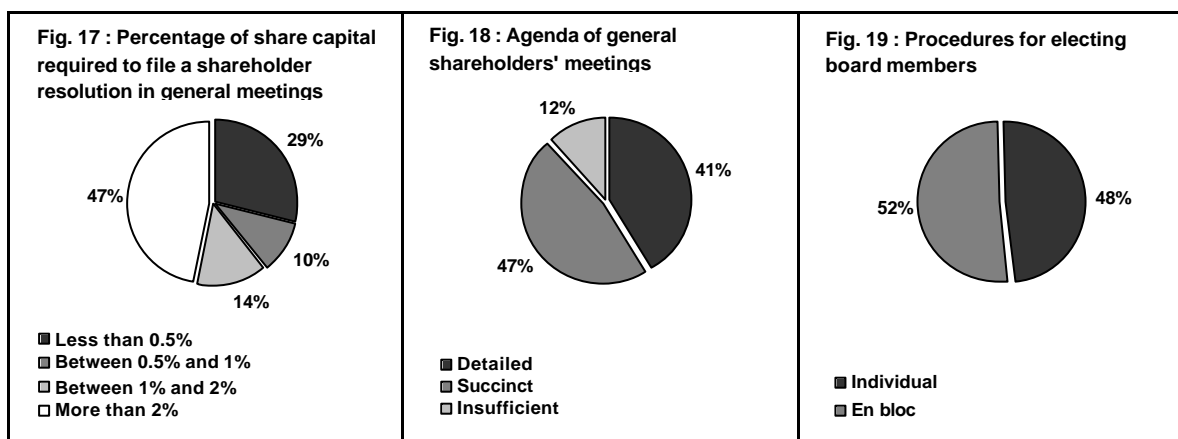
concerning new board members or the description of the structure and characteristics of stock option plans for which the company requests authority to create new conditional capital.

Codes of best practice in corporate governance specify that board directors should be elected on an individual basis and not en bloc. Although the board of directors generally adopts a collegial work style, it is nevertheless composed of individual members with their specific roles and responsibilities. It is therefore essential that a shareholder be able to express his acceptance or rejection of each candidate on an individual basis.

In evaluating shareholder participation, ethos analysed the following points:

- The percentage of share capital an investor is required to hold in order to put an item to the agenda of a general meeting.
- The quality of information provided in the agenda of general meetings.
- Election and re-election procedures for board directors.

## Results



The results clearly demonstrate that the most fundamental of shareholders' participation rights are frequently neglected or disregarded by Swiss companies.

- Almost 50% of the companies require an investor to hold more than 2% of the capital in order to add an item to the agenda of the general shareholders' meeting.
- Only 41% of the companies provide sufficiently detailed agendas of general meetings.
- Over half the companies elect their board of directors en bloc.

### 3. TRANSPARENCY AND BEST PRACTICE : THE FOUNDATIONS OF CORPORATE GOVERNANCE

If a company wishes to be outstanding in terms of best practice in corporate governance, not only should it achieve the level of transparency required by the SWXDirective, but also apply the entire body of principles enshrined in codes of best practice in corporate governance.

It is of considerable interest to combine the results obtained in section 1 (the SWXDirective transparency requirements) and section 2 (ethos corporate governance rating) of the study carried out on 100 companies. In table 5, the vertical axis corresponds to the level of transparency whereas the horizontal axis refers to standards of best practice.

The “**leaders**” in corporate governance, i.e. the companies that achieved the highest standards of transparency and best practice, are therefore located in the top right hand segment of the table. The “**laggards**” are in the bottom left hand corner. Companies who achieve a satisfactory level of transparency without adequately applying principles of best practice may be qualified as “**Window dressers**” and are to be found in the top left hand segment. Finally the “**secret implementers**” (bottom right hand segment) show willingness to apply principles of best practice but remain reluctant to disclose information in a transparent manner.

In general, we can observe that companies listed on the SMI index demonstrate a higher standard of corporate governance. The five leaders amongst the major companies are UBS, Swiss Re, Credit Suisse Group, Zurich Financial Services and Unaxis. At the other end of the spectrum, we find Société Générale de Surveillance, Swatch, Richemont, Kudelski and Roche, companies which are seriously lagging in matters concerning best practice.

**Table 4 : Leaders, Laggards, Window Dressers and Secret Implementers**  
(top five in each category)

<b>Leaders</b>	<b>Laggards</b>	<b>Window dressers</b>	<b>Secret implementers</b>
UBS	Zehnder	Schindler	Converium
Swiss Re	Conzzeta	Jelmoli	Straumann
CS Group	Belimo	Basler KB	Leica Geosystem
Zurich Fin. Serv.	EMS Chemie	Datwyler	Givaudan
Unaxis	Edipresse	Lindt & Sprüngli	---
Leaders: Good transparency and good corporate governance practice Laggards: Lack of transparency and corporate governance unsatisfactory Window dressers: Good transparency but corporate governance unsatisfactory Secret Implementers: Lack of transparency but good corporate governance practice			



## 4. IMPROVEMENTS TO THE SWX-DIRECTIVE AND THE ECONOMIESUISSE CODE

### 4.1 CLARIFYING THE SWX-DIRECTIVE

The manner in which leading companies responded to transparency and best practice requirements in 2003 indicates that various improvements to the SWX-Directive would be welcome.

#### - The SWX-Directive as a whole

It is highly recommended that all sections of the Directive be mandatory. At present, the section on compensations is the only mandatory section.

Furthermore, it would be appropriate that the requested information be set out in a special chapter of the annual report, the structure of which corresponds exactly to the SWX-Directive format.

Finally, it would be useful for the investor to be informed of any items in the SWX-Directive that are not applicable to the company in question.

#### - Section 2 (Capital structure) and section 6 (Shareholders' participation rights)

Several companies confused issues relevant to limitations on transferability of shares (section 2) and limitations on voting rights (section 6). It would therefore be advisable to disclose information concerning these issues in a single section.

#### - Section 3 (Board of Directors)

In order to better assess the availability of directors, it would be useful to know the exact number of mandates held by individual board members, and not merely the most significant mandates. In pursuance of the same vein, it would also be useful to know the attendance rate of individual directors at board and committee meetings, as is the trend in the United States.

#### - Section 5 (Compensation)

With regard to section 5 (compensation), several improvements are necessary to enable the investor to form a clear picture of companies' remuneration practices, in particular remuneration principles and procedures as well as the amounts paid-out.

In particular, the following ameliorations should be considered :

- Item 5.1, "Content and method of determining the compensations and the shareholding programmes" should clearly set out the information to be disclosed by the companies. This would allow investors to understand the procedures and the competencies regarding determination of remuneration, as well as characteristics and objectives of remuneration policies. The company should clearly communicate the performance criteria that should be attained before bonuses or other variable remunerations can vest.
- The SWX-Directive requires that total remunerations be disclosed. However, it only requires the disclosure of the number of allotted shares and options, but not of their value. As a result, some companies disclosed remuneration including the value of options and shares, whereas others did not. In order to enhance comparability of remuneration, the number and value of allotted options and shares should systematically be disclosed and included in the total individual remuneration.

- At present, the highest total compensation paid to a director should be disclosed, irrespective of whether the recipient is a member of the management board or not. In contrast, a company is not required to disclose the highest total compensation paid to a member of the management board unless that person is a member of the board of directors. In order to avoid such unequal treatment, the SWX Directive should make provision for the disclosure of the highest total compensation paid to a member of the management board. A further step would be the disclosure of individual remunerations (of directors and management board members), a step that some companies have taken on their own initiative.

### **Section 8 (Auditors)**

A breakdown of additional honorariums (non-audit fees) would greatly facilitate the readers' ability to assess the auditors' level of independence.

## **4.2 ENHANCING THE ECONOMIESUISSE CODE**

The Swiss code of best practice for corporate governance published by economiesuisse in 2002, is a much appreciated body of recommendations to Swiss companies. However, practice indicates that various additions would be welcome so that the document can become a reference for international investors.

First, the Code would be considerably enhanced if, consistent with foreign codes, it applied the principle of "Comply or explain" which is a fundamental condition to compliance.

The present version does not make reference to the equal treatment of shareholders. However, the "one share, one vote" principle is an essential element of corporate governance from the shareholders' point of view.

In the section on the board of directors, the definition of a board director's independence could be further elaborated. For instance, it would be wise to specify (as in the British Combined Code) that when a director holds office for more than 10 years, he may no longer be considered independent. Furthermore, the present Code recommends that the majority of board members be non-executive as opposed to independent.

Finally, it would be commendable that a revised version of the Code clearly recommend a corporate structure that prevents a single person from assuming the joint functions of Chairman of the board of directors and CEO.



## ANNEXES

### Annex 1: List of 100 companies analysed

Rank	Name		Rank	Name	
1	ABB	SMI	51	NATIONALE SUISSE	
2	ACTELION		52	NESTLE	SMI
3	ADECCO	SMI	53	NOBEL BIO CARE	
4	AFFICHAGE		54	NOVARTIS	SMI
5	ALLREAL		55	OZ	
6	BACHEM		56	PARGESA	
7	BALOISE	SMI	57	PHOENIX MECANO	
8	BANK COOP		58	PHONAK	
9	BANK SARASIN		59	PSP	
10	BASELSTADT KB		60	PUBLIGROUPE	
11	BASLER KB		61	REG REAL ESTATE	
12	BEKB / BCBE		62	RICHEMONT	SMI
13	BELIMO		63	RIETER	
14	BERNA BIOTECH		64	ROCHE	SMI
15	BOBST		65	SAIA-BURGESS	
16	BON APPETIT		66	SARNA KUNSTSTOFF	
17	BUCHER		67	SAURER	
18	CHARLES VOEGELE		68	SCHINDLER	
19	CIBA SPECIALITES	SMI	69	SERONO	SMI
20	CLARIANT	SMI	70	SEZ	
21	CONVERIUM		71	SGS	SMI
22	CONZZETA		72	SIA ABRASIVES	
23	CS GROUP	SMI	73	SIEGFRIED	
24	DAETWYLER		74	SIG	
25	EDIPRESSE		75	SIKA	
26	EMS-CHEMIE		76	ST GALLER KB	
27	FORBO		77	STRAUMANN	
28	GALENICA		78	SULZER	SMI
29	GEBERIT		79	SWATCH	SMI
30	GEORG FISCHER		80	SWISS LIFE	SMI
31	GIVAUDAN	SMI	81	SWISS PRIME SITE	
32	GURIT-HEBERLEIN		82	SWISS RE	SMI
33	HELVETIA PATRIA		83	SWISSCOM	SMI
34	HIESTAND		84	SWISSFIRST	
35	HOLCIM	SMI	85	SWISSLOG	
36	INFICON		86	SYNGENTA	SMI
37	JELMOLI		87	SYNTHES-STRATEC	
38	JULIUS BAER	SMI	88	TAMEDIA	
39	KOMAX		89	TECAN	
40	KUDELSKI	SMI	90	UBS	SMI
41	KUEHNE & NAGEL		91	UNAXIS	SMI
42	KUONI		92	VALIANT	
43	LEICA GEOSYSTEMS		93	VALORA	
44	LIECHTENSTEIN LBK		94	VONTOBEL	
45	LINDT & SPRUENGLI		95	VP BANK	
46	LOGITECH		96	ZEHNDER	
47	LONZA	SMI	97	ZSCHOKKE	
48	LUZERNER KB		98	ZUEBLIN IMMOB	
49	MICRONAS		99	ZUGER KB	
50	MOEVENPICK		100	ZURICH FIN SERV	SMI

## **Annex 2: Methodology of evaluation of Compliance with the SWX-Directive**

### **Items and evaluation**

The list of evaluated items is based on the SWX-Directive annex concerning information relevant to corporate governance. The latter specifies the type of disclosures required of companies that fall within the scope of the Directive. A total of 68 items was drawn up. Even those items that are not applicable to certain companies (for instance, the item concerning dividend-right certificates does not apply to a company that does not issue them) are carefully analysed.

For each applicable item, disclosure is evaluated as follows:

- Disclosure fully complies with the requirements of the SWX-Directive (2 points)
- Disclosure partially complies with the requirements of the SWX-Directive (1 point)
- Insufficient or no disclosure (0 points)
- Disclosure specifies that the item is not applicable (2 points)
- Failure to disclose that the item is not applicable (1 point)

### **Calculation of final rating**

The number of points is multiplied by the weighting attributed to the item concerned. Items are weighted according to their importance and the level of detail.

The maximum rating obtainable is 100 points. The ethos foundation considers that a company must obtain at least 80 points to be deemed sufficiently transparent vis à vis the SWX-Directive. Nevertheless, to be truly in compliance with the SWX-Directive, a company must also have disclosed all information required in section 5 (remuneration), i.e. the mandatory section.

## **Annex 3: Methodology of ethos' "Corporate Governance" rating**

### **Subjects evaluated**

Five main subjects are evaluated :

- 1) Information (2 items)
- 2) Capital structure (3 items)
- 3) Board of directors (5 main items and several sub-items)
- 4) Auditors (2 items)
- 5) Shareholders' participation rights (3 items)

Each item is rated on a scale of 0 to 3.

### **Weighting**

For the purposes of this study, the five subjects are weighted as follows :

- 1) Information: 20%
- 2) Capital structure: 15%
- 3) Board of directors: 35%
- 4) Auditors: 10%
- 5) Shareholders' participation rights: 20%

### **Initiatives and controversies**

The intermediate rating obtained from an assessment of the five areas may be adjusted by no more than 20% considering events that ethos deems positive (initiatives) or negative (controversies) which fall into one of the three following categories:

- 1) The quality of dialogue between the company and ethos
- 2) Divergence of voting recommendations between ethos and the company's board of directors at annual or extraordinary general meetings.
- 3) Specific events that occurred within the last 12 months.

### **Calculation of the ethos' 'Corporate Governance" rating**

For the purposes of this study the ethos rating is expressed in percentage points, the highest rating being 100%.