

## **Scorecard for German Corporate Governance<sup>®</sup>**

DVFA Evaluation Method based on the 'German Corporate Governance Code'

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# **'Scorecard for German Corporate Governance<sup>®</sup>**

## **- DVFA Evaluation Method based on the 'German Corporate Governance Code'-<sup>1</sup>**

### **Objective**

In addition to the traditional evaluation methods, Corporate Governance is an increasingly important part of modern company analysis for financial analysts and investors. 'Corporate Governance particularly relates to the proper functioning of the management and supervisory boards, their co-operation and the control of their actions'.<sup>2</sup> Equally, the behavior of companies regarding information and transparency is of substantial importance for their evaluation that is increasingly characterized by non-material assets. Companies which want to be successful in the competition for equity and debt capital have to satisfy demanding Corporate Governance standards over and above their legal obligations. Recent research results provide reasonable evidence that investors attribute higher valuations to companies which follow demanding Corporate Governance standards.<sup>3</sup>

The 'Scorecard for German Corporate Governance<sup>®</sup>' serves as a practical analytical tool for financial analysts and investors. The Scorecard was developed against the background of the 'German Corporate Governance Code'<sup>4</sup> (as introduced by the 'German Government Commission on Corporate Governance' on February 26<sup>th</sup>, 2002) as well as other internationally relevant 'best practice standards'.

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<sup>1</sup> Available on-line under <http://www.dvfa.de>

<sup>2</sup> Baums, Theodor: 'Bericht der Regierungskommission Corporate Governance - Unternehmensführung, Unternehmenskontrolle, Modernisierung des Aktienrechts', Frankfurt am Main, 2001, Page 6; English translation of the summary of recommendations available at: <http://www.shearman.com>

<sup>3</sup> Gompers, Paul A./Ishii, Joy L./Metrick, Andrew: 'Corporate Governance and Equity Prices', National Bureau of Economic Research, Working Paper No.8449, August 2001; 'Investor Opinion Survey', published by McKinsey & Company, June 2000

<sup>4</sup> Available on-line under: <http://www.corporate-governance-code.de>

## **Basis**

German Corporate Governance is on the one hand contained in several laws, e.g. KonTraG, KapAEG, KapCoRiLiG, 'Takeover Law' and the '4<sup>th</sup> Financial Market Promotion Act'. These company and capital market laws cover important internationally recognized Corporate Governance principles. On the other hand, a large number of governance standards not covered in specific laws are an essential part of 'good' Corporate Governance.

This environment of legal and other principles was basis for the work of a 'German Government Commission on Corporate Governance' which issued an official '**German Corporate Governance Code**' on February 26<sup>th</sup>, 2002. The legal obligation of the 'Law for Transparency and Publicity' (TransPuG) to pursue the 'Shall Recommendations' of this Code is expected to become mandatory in August 2002. According to the 'Comply or Explain' principle contained in this law, German listed companies have to either comply with the 'Shall Recommendations' of the Code or publish any deviation thereof at least annually.

## **The 'Scorecard for German Corporate Governance<sup>©</sup>' as DVFA evaluation method for the practical analytical work**

With the adaptation of the 'DVFA Scorecard' to the new Code, the 'DVFA Working Group Corporate Governance'<sup>5</sup> provides financial analysts and investors with a practical evaluation method of the governance displayed by listed German companies.

The following details govern the Scorecard:

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<sup>5</sup> Members:

PD Dr. Alexander Bassen  
Prof. Dr. Hans-Joachim Böcking  
Prof. Dr. Otto Loistl  
Christian Strenger

- To facilitate the reference to relevant points of the 'German Corporate Governance Code', the '**Shall Recommendations**' are printed **in bold type** in the brackets of a particular criterion point of the Scorecard, while '*Should Suggestions*' are pointed out *in italics*.
- The scores for the individual criteria and the total score can be calculated using 'MS Excel' standard software. By marking the relevant level of fulfillment (column 1) one can evaluate comprehensively and systematically the actual compliance with '**Shall Recommendations**' and '*Should Suggestions*' of the Code as well as other 'best practice standards' of 'good' corporate governance.
- The proposed **Standard Weighting** (column 2) envisages that companies fulfilling all 'Shall Recommendations' of the Code and displaying an active Corporate Governance commitment (Criterion I of the Scorecard) achieve already a total score of 75%. A total score of 100% can be achieved by fulfilling the Code's '*Should Suggestions*' as well as other 'best practice standards'. It is therefore likely that companies with demanding governance standards achieve a score of at least 80% to 90%.
- If desired, the proposed standard weighting of individual points can be replaced by an **Individual Weighting** (column 3). The total of all weightings must, however, sum up to 100%.
- If specific questions cannot be answered positively due to company-specific conditions (e.g. particular legal points), the respective fulfillment column (1) should be marked 'yes' and with an 'asterisk' (\*). This should naturally not take place if this would violate principles of 'good' governance. In line with the 'Comply or Explain' approach of the Code such deviations shall be marked in the column 'Information Source'.
- **Future updates of the Scorecard** will be made on a timely basis, particularly in case of changes in the 'German Corporate Governance Code' and the legal environment, but also in case of significant developments of corporate governance standards.