POSITION PAPER

ESBG position paper on the proposal for a Directive of the European Parliament and of the Council amending Directive 2007/36/EC as regards the promotion of long-term involvement of shareholders and Directive 2013/34/EU with regard to certain elements of the Declaration of corporate governance

ESBG (European Savings and Retail Banking Group)

Rue Marie-Thérèse, 11 - B-1000 Brussels

ESBG Transparency Register ID 8765978796-80

October 2014

ESBG

The European Savings and Retail Banking Group (ESBG) takes the opportunity to comment on the proposal Directive of the European Parliament and of the Council amending Directive 2007/36/EC as regards the promotion of long-term involvement of shareholders and Directive 2013/34/EU with regard to certain elements of the Declaration of corporate governance (hereinafter draft Directive).

General comments

ESBG shares the objectives of the draft Directive, i.e. an improved activity from the shareholders, increased openness and other actions that promote shareholders engagement and facilitate for the cross-border shareholders possibility to influence.

However, the potential positive impact should still be carefully assessed.

ESBG is indeed concerned about a significant risk of additional administrative burdens on the equity market and increased costs for the stakeholders without corresponding benefit for the market, especially since the level of detail is rather high in certain areas. This is why a deeper and more thorough analysis of the socioeconomic benefits should be undertaken before going forward with the proposal in order to assess whether the proposed measures are really necessary.

Whether the harmonisation objective could be fulfilled can also be questioned due to several reasons, e.g. the nature of a directive and the imprecision of some provisions (despite the level of details) might lead to a differentiated treatment and implementation in Member States. It can also be pointed out that there is no common European definition of “shareholder”, and that there is no common European book-entry system or even common rules on such systems.

One of the Commission’s arguments for common rules is the increase in cross-border interests, which would entail a need for harmonised rules between Member States. As the equity market is globalised rather than pan-European and the directive would only apply to activities within Member States, the increased demands (e.g. regarding the transmission of cross-border information) run the risk of giving those asset managers and intermediaries which operate outside EU a competitive advantage.

It may also be questioned that detailed rules regarding an obligatory engagement policy and its public disclosure from institutional investors and asset managers will prevent excessive short-term risk-taking and manage potential conflicts of interest. Many of these investors located in countries where ESBG members operate already have such policies and the flow of information to their customers is self-regulated through the demands from the customers.

When it comes to small shareholders the vast majority only looks at the return and see the equity investment as an alternative to a savings account. Enhanced information flows and evident policies from investors and asset managers will most probably not change their attitude on this and will therefore not serve its purpose. As a result ESBG is of the opinion that the rules of information should be limited to larger shareholders, defined above a certain threshold.

Moreover, the content of the draft directive seems not to be adapted to the two tier system since the term ‘Directors’ is used both in the sense of Board Members and for members of executive management. This needs to be clarified.

ESBG would also like to attract your attention to the fact that the proposal addresses, when considering the shareholders rights, the situation of commercial companies, because "shareholders" are defined as the people who hold shares. And "shares" are considered to be "stocks". Some banking institutions which are members of ESBG are not stock companies, but rather cooperatives, foundations and mutual entities; the capital of cooperatives and mutuals belongs to a multiplicity of partners, each one having a share equivalent to the others, and the capital of foundations does not belong to any one legally speaking as it is allocated to social goals and no dividends are paid. Therefore, some of the provisions which are contemplated in the draft directive are not applicable as such. As a consequence, our proposals made below should be adapted in particular with regards to the limitation of the identification of shareholders to major stakes, the documents which represent the partnership link to our entities, and the proxy voting rights by a depositary bank.
Lastly the draft directive would deserve to be better coordinated with other regulatory initiatives within the European Union (and the EEA).

Specific comments

1. Identification of shareholders

Article 3a of the draft directive raises a matter of principle which leads to suggest that this scheme should be removed because it does not respect the fundamental difference between bearer shares and registered shares. In case an identification process would however go forward, ESBG would plead at least for the following clarifications.

The expressed obligation for intermediaries raises a variety of questions that are not answered in the draft. Only a few countries in the EU have established national systems for the identification of shareholders. European standards would be required - in parallel to the general meeting standards.

- In order to reduce the practical problems for intermediaries, ESBG proposes to limit the identification obligations to major stakes, for instance setting up a threshold of 0.5 percent. Those companies that wish to reach the shareholder below this threshold can achieve this by negotiation with the intermediaries.

- It remains unclear how the intermediary is relieved of its obligation to name the shareholder if the shareholder opposes to his disclosure. It also remains open how the transmission of data over long chains of intermediaries should take place without delay. The SWIFT data system which has been suggested by the industry would have been useful to serve this purpose.

- Paragraph 2 establishes in fact an obligation from the institutional shareholder to apply the Legal Entity Identifier (LEI) in order to meet the requirement of the "unique identifier". So far only in the EMIR regulation 648/2012 there is such a binding obligation for non-financial counterparties with regards to derivative transactions. This means that only a small number of companies currently have an LEI.

- The right to information is also formulated in too broad a manner. In addition to the expected strong efforts, which a single briefing would include, repeated update requests of listed companies could happen due to the fact that share portfolios change rapidly. In practice, this would be even more burdensome for the institutions.

Therefore, there should at least be a reasonable limit to the obligation to provide information, such as setting a limit at the 'Record Date' prior to the general meeting so that the updating obligations would not apply.
The completeness and accuracy of the data are a responsibility of the customer who must act in his own interests in this context. There is no practical way of ensuring this at the level of the institutions.

- Paragraph 3 of Article 3a states: "(...) The company and the intermediary shall ensure that natural persons are able to rectify or erase any incomplete or inaccurate data and shall not conserve the information relating to the shareholder for longer than 24 months after receiving it."
  This article does not seem to take into account the fact that some shareholders are long-term holders, so that, from the point of view of both the company and the intermediary, this temporal limitation to the data retention of shareholders forces them to get rid of data that would have to be requested again.
  Also, since the term is computed from the receipt of the information, this deadline would be difficult to manage and control. Alternatively, one could set a deadline for the removal of information from the moment on which the shareholder loses all of the shares of the company.

2. **<u>Transmission of information</u>**

According to Article 3b of the draft Directive, the intermediaries will be obliged in the future to provide information on the shares held throughout the EU, for example with respect to the general meetings or capital measures (in some countries, it is mandatory only for some companies based in the Member State).

Details of this obligation, such as the question of the transmission medium, are not addressed, and therefore they are left to be decided upon by the European Commission (in the form of implementing acts), which leads to uncertainties.

ESBG suggests cancelling the obligation of reporting any information that is meant for all shareholders. Indeed the information should be limited to general information and not individually adapted to each shareholder. As a further argument in favour of this approach, it can be noted that retail shareholders seem not to be specifically interested in such information; moreover those who have expressed an interest in receiving this information are provided with it.

On a side note, the question of the translation of the information (at least in English) received from the issuer by the intermediary is not addressed. In order that the intermediary does not face questions from the investors to which it will not be able to reply, an obligation of translation should be imposed on the issuer.

Lastly the cost of the transmission of the information should be borne by the issuer, and not by the intermediary.

3. Facilitation of the exercise of shareholder rights

This section is quite detailed, e.g. the disclosure of information on the voting (what and why) from the investor at every general meeting. Such information is not always in the interest of the investor, the company and/or the shareholders. In order to establish such disclosure clauses, it ought to be less detailed.

In Article 3c, the so-called proxy voting right, i.e. the exercise of the voting right by the custodian bank, is explicitly mentioned as a possible option for the national legislative bodies. ESBG advocates for preserving the optional proxy voting system which exists in some countries (for instance, § 135 of AktG – German Stock Corporation Act) and which enables institutions to decide whether they offer this service to their customers. It is important to note that the customers do not necessarily value this service, which requires strong efforts.
Moreover, in case this new service would be put in place, the confirmation of the vote has to be undertaken towards the individual custody client. As issuers will have to confirm the votes by the shareholders (or on their behalf), the custodian bank will be in charge of reporting the votes to the shareholder if the custodian bank itself has exercised the voting rights. The method of how this should be done is not specified.

4. Transparency on costs

According to Article 3d of the proposed Directive, Member States should allow intermediaries to collect on behalf of the issuer charges from the shareholders, the companies and other intermediaries for services included in Chapter IA "Identification of shareholders, transmission of information and facilitation of exercise of shareholder rights".

In principle, Article 3d is welcomed as it provides a balanced cost distribution between issuers and intermediaries with regards to the right to reimbursement for expenditures. However the proposal should, in our opinion, point out even more clearly that the respective national rules regarding the relationship between companies and intermediaries have cross-border effects. The advantage of reimbursement regulation is that for issuers and intermediaries there would be standardised rules on reimbursement of costs across the entire market, which should consequently make negotiations unnecessary.
In order to prevent costs being passed on as a flat rate to shareholders in practice, for instance also to those who are not affected by a capital measure, it should be clarified that the issuer and other senders of the information, which is addressed to shareholders, are obliged to bear the costs.

5. Right to vote on the remuneration policy

In the draft directive (Article 9a), the proposed voting rights of the shareholders on the remuneration policy of listed companies go far beyond the national legal provisions.

- In Germany for instance, the proposed voting rights go far beyond the German legal provisions (§ 120(4) of the AktG and the German Corporate Governance Code) on the participation rights of the general meeting. Unlike the reasoning of the draft directive, such a right to vote would certainly bump into the "key role of the supervisory board in dualistic systems". It would lead to an essential loss of powers of the Supervisory Board and to a weakening of the dualistic organisational structures of German stock corporations.

- In Spain, in the Royal Legislative Decree 1/2010 of 2 July, whereby the revised text of the Law of Corporations (LSC) is approved, the directors of the companies, except in the case an executive and solely in connection with its executive functions, shall not sign a contract with the society. The directors are appointed by the general meeting (to be checked) or, where appropriate, co-opted by the board, for the statutory period, or failing that, for the maximum legal term, and its system of remuneration in accordance with Article 217 LSC, must be stated in the bylaws.
  As for notice periods or payment related to its rescission, it should be noted that according to Article 223 of the LSC, administrators can be removed from office at any time by the general meeting, even though the removal does not appear in the agenda, and that, according to Article 224 of the same rule, administrators who were disqualified on account of legal prohibition shall be immediately replaced at the request of any shareholder.

Therefore, the proposal of the European Commission (Article 9a, paragraph 3, fourth indent) for the policy "to indicate the main terms of the contracts of directors, including its duration and the applicable notice periods and payments linked to termination of contracts" should be removed in order to prevent legal uncertainty. ESBG considers that it should not be the task of the general assembly to discuss the terms of the contracts of directors.

Paragraph 4 of Article 9a provides that, once approved by shareholders, Member States shall ensure that the policy is made public and available on the website of the company. For the specific case of financial institutions, this obligation of disclosure of remuneration policy goes beyond the provisions of Article 450 of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (RRC), which establishes the minimum information which is to be disclosed concerning institutions' policies and remuneration practices, without indicating that the policy in its entirety should be disclosed.
Therefore, ESBG suggests the adaptation of paragraph 4 to align with the obligation set up in the CRR.

6. <u>Information to be provided in the report related to remuneration and the right to vote on it</u>

For the reasons pointed out in relation to the aforementioned Article 9a, in the first subparagraph of paragraph 1, Article 9b, ESBG believes that we should not refer to the recruitment, but to the appointment of the directors. Therefore, the following rewording is proposed: "1. Member States shall ensure that the company draws up a clear and understandable remuneration report, providing a comprehensive overview of the remuneration, including all benefits in whatever form, granted to individual directors, including to newly ~~recruited~~ **appointed** and former directors, in the last financial year. (...)"

ESBG also suggests reviewing the wording of point (b) of paragraph 1, Article 9b, since the current wording may lead to confusion as to the nature of the office of director to establish: "(...) and to change in the average remuneration of full time employees of the company other than directors; (...)".

7. Right to vote on related party transactions

Regarding the proposals on related party transactions (Article 9c), it should be noted that e.g. the obligatory report from an independent third party is in listed companies already taken care of by existing rules of internal and external audit assessment and other forms of control.

Furthermore, the obligatory approval from general meetings for certain transactions ("5% rule") does not seem to be appropriate and would deserve to be established in a more proportionate way. A "10% rule" as already experienced in some countries (such as in Spain, based on the recommendation of the Committee of Experts on Corporate Governance of the Spanish National Securities Market Commission – CNMV) seems to be more appropriate and proportionate.
ESBG also believes that the exemption from the shareholders' approval of transactions between companies which are members of the same group should constitute a rule and not an exception which may or may not be granted by Member States. Otherwise, this requirement may work like a strait-jacket in relation to transactions within a group of companies.

About ESBG (European Savings and Retail Banking Group)

ESBG brings together savings and retail banks of the European Union and European Economic Area that believe in a common identity for European policies. ESBG members support the development of a single market for Europe that adheres to the principle of subsidiarity, whereby the European Union only acts when individual Member States cannot sufficiently do so. They believe that pluralism and diversity in the European banking sector safeguard the market against shocks that arise from time to time, whether caused by internal or external forces. Members seek to defend the European social and economic model that combines economic growth with high living standards and good working conditions. To these ends, ESBG members come together to agree on and promote common positions on relevant matters of a regulatory or supervisory nature.

ESBG members represent one of the largest European retail banking networks, comprising of approximately one-third of the retail banking market in Europe, with total assets of over €7,300 billion, non-bank deposits of €3,480 billion and non-bank loans of €3,950 billion (31 December 2012).

European Savings and Retail Banking Group – aisbl
Rue Marie-Thérèse, 11 ▪ B-1000 Brussels ▪ Tel: +32 2 211 11 11 ▪ Fax : +32 2 211 11 99
Info@wsbi-esbg.org ▪ www.esbg.eu

Published by ESBG. September 2014.