

Opinion of the European Economic and Social Committee on the ‘Proposal for a Directive of the European Parliament and of the Council amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement and Directive 2013/34/EU as regards certain elements of the corporate governance statement’

COM(2014) 213 final — 2014/0121 (COD)

(2014/C 451/14)

Rapporteur: **Mr Smyth**

On 16 April and 6 May 2014 respectively, the European Parliament and the Council decided to consult the European Economic and Social Committee, under Articles 50 and 114 of the Treaty on the Functioning of the European Union, on the:

Proposal for a Directive of the European Parliament and of the Council amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement and Directive 2013/34/EU as regards certain elements of the corporate governance statement.

COM(2014) 213 final — 2014/0121 (COD).

The Section for the Single Market, Production and Consumption, which was responsible for preparing the Committee’s work on the subject, adopted its opinion on 23 June 2014.

At its 500th plenary session, held on 9 and 10 July 2014 (meeting of 9 July 2014), the European Economic and Social Committee adopted the following opinion with 188 votes in favour and 5 abstentions.

1. Conclusions and recommendations

1.1 The Commission’s proposals to amend the Shareholder Rights Directive should be seen as part of a longer journey towards a more stable, sustainable corporate governance and investment environment in Europe. At the heart of these proposals is the view that if shareholders can be encouraged to take a more long-term perspective, then this will create a better operating environment for listed companies.

1.2 The EESC supports the provisions to the Shareholder Rights Directive, especially those that seek to strengthen the link between the remuneration awarded to directors and the long-term performance of companies.

1.3 The EESC notes that in its impact assessment the Commission argues that its proposals will lead to only a marginal increase in the administrative burden on listed companies. It will be important to assess this balance during the ex post evaluation of the Directive.

1.4 The EESC accepts the argument that, by creating more transparency on the impact of investment policies, investors will make more informed decisions and are likely to become more engaged with their investee companies. This should lead to better long-term performance by listed companies.

1.5 Since the onset of the financial crisis policymakers have embarked on the challenge of changing the culture in the European corporate and financial sectors away from short-term performance towards a more sustainable long-term investment perspective. Insofar as such a culture change can be achieved through regulation, then the Commission is moving in the right direction.

2. Background to the Directive

2.1 This proposed Directive from the Commission should be seen in the context of other initiatives to improve the long term financing of the European economy. At its core is the conviction that the encouragement of a more long-term perspective by shareholders will insure a better operating environment for listed companies. These proposals represent part of the outcome of an extensive corporate governance consultation process with stakeholders. In 2010, the Commission issued a Green Paper on 'corporate governance in financial institutions and remuneration policies' ⁽¹⁾. This was followed up by another Green Paper 'the EU corporate governance framework' ⁽²⁾ in 2011. These consultations then led to the publication in 2012 of the 'Action Plan: European company law and corporate governance — a modern legal framework for more engaged shareholders and sustainable companies' ⁽³⁾.

2.2 The Directive draws upon an impact assessment which addresses shortcomings in the relationship between the main corporate governance protagonists — the so-called principle-agent relationship. This refers to the relationship between agents (directors) and principles (shareholders such as institutional investors, asset managers and proxy advisers). It identifies five of these shortcomings as follows: (i) lack of sufficient engagement of institutional investors and asset managers; (ii) inadequate linkages between pay and performance of directors; (iii) lack of shareholder oversight on related party transactions; (iv) inadequate transparency of proxy advisers; and (v) difficult and costly exercise of rights flowing from securities for investors.

2.3 For each of these issues, the Commission considers the relevant policy options and chooses five sets of policy measures as follows:

- 1) Mandatory transparency of institutional investors and asset managers on their voting and engagement and certain aspects of asset management arrangements;
- 2) Disclosure of the remuneration policy and individual remunerations, combined with a shareholder vote;
- 3) Additional transparency and an independent opinion on more important related party transactions and submission of the most substantial transactions to shareholder approval;
- 4) Binding disclosure requirements on the methodology and conflicts of interests of proxy advisers;
- 5) Creating a framework to allow listed companies to identify their shareholders and requiring intermediaries to rapidly transmit information related to shareholders and to facilitate the exercise of shareholder rights.

3. The Directive's measures

3.1 In terms of shareholder transparency the Commission requires institutional investors to disclose how the equity strategy is aligned with their liabilities and how it contributes to the longer term performance of the assets. In addition, if the institutional investor utilises the services of an asset manager, there will be required to disclose the key elements of this arrangement, such as the alignment of the asset managers and institutional investors, investment strategies, the time horizon of the strategy, the evaluation of the asset managers' performance, the targeted portfolio turnover etc. Asset managers will likewise have to disclose to institutional investors every six months, how their investment strategy is operating in accordance with the agreed approach.

3.2 On the link between directors' pay and performance the Commission is concerned that the lack of effective oversight of directors' remuneration may detract from the longer term performance of the business. Boards or Supervisory Boards develop remuneration policy. Listed companies will be required to publish detailed information on remuneration policy and the remuneration of individual directors. Shareholders will have the right to approve the remuneration policy and also the operation of the policy in the preceding year. The proposed Directive leaves the level and conditions of remuneration to the company and its shareholders.

⁽¹⁾ COM(2010) 284 final.

⁽²⁾ COM(2011) 164 final.

⁽³⁾ COM(2012) 740 final.

3.3 The issue of related party transactions centres on the view that shareholders normally do not have access to sufficient information about such proposed transactions nor adequate mechanisms to oppose (abusive) transactions. Listed companies will therefore be required to seek the approval of shareholders in respect of related party transactions which represent more than 5 % of the companies' assets. They will also have to announce such transactions if they are greater than 1 % of their assets and have the transactions audited by an independent third party. There will be exemptions for transactions between a company and members of its group that are fully owned by the company.

3.4 Proxy advisors provide investors with recommendations on how to vote in the general meetings of listed companies. The use of proxy advisors has arisen mainly due to the complex issues involved in equity holdings of investors, particularly on a cross-border basis. Proxy advisors provide recommendations to investors with highly globalised and diversified portfolios, and exert an important influence on voting behaviour and hence on corporate governance. In its impact assessment research the Commission finds evidence that casts doubt on the quality and accuracy of advice provided by proxy advisors as well as their handling of issues relating to conflicts of interest. There is no EU level regulation of these proxy advisors although some Member States have non-binding codes of conduct. Proxy advisors will be required to undertake measures to guarantee that their voting recommendations are accurate and reliable, and based on a thorough analysis of all the relevant information and are not affected by any actual or potential conflicts of interest. It is understood that proxy advisors are currently seeking ESMA approval for a voluntary code of conduct; this is to be welcomed.

3.5 Investors, particularly those with cross-border equity holdings, face difficulties in exercising the rights flowing from their shares. These difficulties stem mainly from the ability of companies to identify investors correctly, the lack of timely transmission of information from companies to shareholders and price discrimination behaviour in cross-border holdings. Member States will be required to ensure that intermediaries offer listed companies the ability to identify their shareholders. Listed companies will be required, if they choose not to communicate directly with shareholders, to provide and deliver information relating to the exercise of rights flowing from shares to an intermediary in a standardised and timely manner. Intermediaries, in turn, are required to facilitate the exercise of shareholder rights, including voting rights, by or on behalf of shareholders, and to inform shareholders accordingly.

4. Comments on the Directive

4.1 The Commission argues that the measures set out in the proposed Directive are likely to lead to only a marginal increase in administrative burden of listed companies. To the extent that they place a requirement on companies to provide timely and relevant information to shareholders, they represent good practice and should therefore be seen in that light. In the case of smaller listed companies, the EESC has concerns about the possibility of an additional administrative burden. Although the Commission commits to undertake an evaluation of the Directive after five years of its operation the EESC believes that, with the likelihood that the proposals will not come into effect for at least another 18 months, such an evaluation should be undertaken earlier.

4.2 On the issue of remuneration policy and the link between pay and performance of directors, the EESC supports the Commission proposals to improve shareholder oversight of directors' remuneration⁽⁴⁾. While the level of remuneration to be paid will remain a matter for the Board, the requirement of a shareholder vote should increase the level of engagement between the Board and its shareholders.

4.3 The argument that, by creating more transparency on the impact of investment policies, investors will make more informed decisions and are likely to become more engaged with their investee companies is logical. If they succeed in engendering longer term shareholder engagement, they should help to improve the efficiency and performance of companies.

⁽⁴⁾ OJ C 271 of 19.9.2013, p. 70.

4.4 These proposals are consistent with those elements of the Capital Requirements Directive ⁽⁵⁾ and Regulation (CRD IV) ⁽⁶⁾ that deal with remuneration and also complement existing rules governing institutional investors and asset managers under the UCITS Directive, MIFID and AIFM. This Directive should be evaluated in the context of this much broader reformed regulatory environment.

4.5 In addition, these proposals sit well in the overall EU corporate governance framework that allows Member States to operate a framework that is more closely aligned to their individual customs and practices. The explicitly cross-border focus of some of the Directive's proposals underlines the need for a set of EU transparency and engagement rules.

4.6 While accepting that for the most part, the proposed revisions to the Shareholder Rights Directive are aimed at fostering better long-term shareholder engagement, the EESC believes that such long-term engagement should involve all stakeholders, including employees and suggests that the Commission should reflect on how better to involve employees in the building of long-term value ⁽⁷⁾.

4.7 In its proposals, the Commission states that 'the overarching objective of the current proposal to revise the Shareholder Rights Directive is to contribute to the long-term sustainability of EU companies, to create an attractive environment for shareholders and to enhance cross-border voting by improving the efficiency of the equity investment chain in order to contribute to growth, jobs creation and EU competitiveness', taken together with the ongoing reform of the financial sector. There is a sea change taking place with the emphasis on changing the culture in the European corporate and financial sectors away from short-term performance towards a more sustainable long-term investment perspective. This will not be a simple task. Insofar as such a culture change can be achieved through regulation, then the Commission is moving in the right direction.

Brussels, 9 July 2014.

The President
of the European Economic and Social Committee
Henri MALOSSE

⁽⁵⁾ OJ L 176, 27.6.2013, p. 338.

⁽⁶⁾ OJ L 176, 27.6.2013, p. 1.

⁽⁷⁾ OJ C 161 of 6.6.2013, p. 35.