‘Shareholder Rights’ Directive- where are we heading to?’

by Markus Ferber, MEP

- check against delivery -

Dear Ladies and Gentlemen,

Thank you for the kind invitation to participate in this event and the opportunity to speak to you today.

“Shareholder rights” is a topic that has been a hot one for quite some time because of several reasons. A couple of weeks ago, we have witnessed the biggest initial public offering in the history of stock exchanges. This was when the Alibaba Group, a giant Chinese online retailer, which has been little known in the western hemisphere before, went public on the New York Stock Exchange. At first glance, one could consider this as a triumph for capital markets in general. However, from a shareholder perspective, it was far from that. In fact, Alibaba only chose New York Stock Exchange as a venue because it allows offering shares with circumcised rights. This creates a 2-class system of shareholders with some very influential shareholders and some so-called “owners” of the company who have no say on how the company is run at all.

This might be an US example, but it is a reminder that shareholder rights are something to fight for. The financial crisis with shareholders supporting managers’ excessive short-term risk taking and paying little attention on how the company is run, offers a different perspective. However, the message is the same: shareholders matter and can make a difference.

The events leading to the financial crisis were on the one hand a shortcoming of the shareholders, who did not paying enough attention, but foremost it revealed serious shortcomings in corporate governance. Hence, the revision of the Shareholder Rights Directive is certainly an important piece in the overall clean-up efforts following the financial crisis. The idea is to tackle corporate governance shortcomings relating to listed companies and their boards, shareholders, intermediaries and proxy advisors (i.e. firms providing services to shareholders, notably voting advice). Many of those corporate governance issues have already been addressed for banks and financial institutions in various pieces of financial markets regulation such as CRD IV and MiFID – to name only a few. Those went along with quite some improvements for instance on the functioning of boards, risk management and remuneration of risk takers in financial institutions. However, the bigger picture needs still some more framing and this is where the Commission's proposal on the Shareholder Rights Directive comes into play.

Apparently, the overall idea of encouraging shareholder engagement and thus making financial markets more attractive for small investors goes well with the EU's overall strategy of boosting investment in investment. Arguably, the whole debate of financing Europe is not only about long-term infrastructure investment, but also about making capital markets more attractive. This goes for both sides: shareholders need an environment that makes it attractive to invest and companies, especially SME, need an environment that makes it attractive to go public and become a listed company. Hence, all measures we are discussing right now need to strike a balance between incentivising shareholders and incentivising companies. I believe that if we do it right, this need not be contradictory.

I am supposed to tell you where we are heading to in terms of the shareholder rights directive. This is easier said than done as we are still in an early stage of the process. The Committee for Economic and Monetary Affairs, which gives an opinion on that file, has just started working on this dossier. The first version of the first draft already exists, but no debate has taken place so far. Hence, it is not easy to predict where we are heading. But of course, there are some aspects that already in this early stage appear to be more controversial than others. Before, I dive into the details, there is one more general remark that I have regarding the whole proposal. It seems as if the whole Commission proposal is very much based on the Anglo-Saxon system of corporate governance and all its specifics. However, for me it is important that we eventually come up with a text that is compatible with all the systems of corporate governance we have in Europe. An example is the area of shareholder identification, which is one of the main points of the directive. For this area we have a couple of rather different approaches between Member States. Those range from central share registries such as the German "Aktionärsbuch" to other approaches that rely more on intermediaries. In the process of the work on this directive we should make sure that the framework we are setting up is able to cater for all those approaches as long as they achieve an appropriate level of shareholder identification across the board. And I believe that we cannot dodge this problem by introducing thresholds either. The Commission's proposal to require identification only above a threshold of 0,1% of holdings will not do the job - simply because the threshold is far too high. Many large companies have a very widespread shareholding with thousands or even ten-thousands of investors not coming even close to the threshold, but only a few dozens or even less above this threshold. So, most certainly introducing such a threshold would severely damage the very idea of shareholder identifica-

tion and thus better shareholder communication. This issue of compatibility with provisions that already exist and work is of course something, we have to keep in mind with all details of the directive. At the moment, I have the impression that the current proposals are leaning too much towards the Anglo-Saxon approach. So that will be an area that needs further investigation.

But now let us have a look at some of the more specifics aspects of the proposal. Probably the one article that will be most hotly debated will be the one on the right to vote on remuneration policies as well as the overall disclosure requirements in the reports that go along with those policies. In general, the idea of giving “a say on pay” to the owners of a company seems to be sensible and very much in line with the principles of a free market economy. Ideally, this can help to ensure that directors' incentives on how to run a company are better aligned with those of the company and its owners. Furthermore, more shareholder accountability might help giving many companies a long-term focus and a better match between performance and pay. The key question on this point will be whether the shareholder’s vote shall be binding or just a strong recommendation. In the German corporate governance system, even a non-binding vote could then be effectively incorporated by the supervisory board. However, the criteria for the remuneration policy the Commission outlines in its proposal seem to be a little too detailed for my taste. The need for explaining pay differentials between directors and employee in the framework of the remuneration policy is such an example. Other factors such as the relation of fixed and variable parts of income or the type of contract concerned are rather obvious and do not need further detailed provisions prescribed by the directive. Unfortunately, I have received signals that some groups want to put even more detailed specifications on the remuneration policy

and the reports into the directive. I find that somehow counter-intuitive given that the whole idea of the directive is giving shareholders influence on the remuneration policy. You are certainly not doing that by drafting the most detailed provisions already in the directive. In the end this might boil down to yet another proposal in the category of "nice idea, but poor execution". We should certainly avoid that.

After all this criticism, there are of course also some points that do make sense in the Commission proposal. For example, it will specify provisions and requirements for intermediaries and proxy advisors that act on behalf of other shareholders. This will help gaining some legal certainty with regards to transparency and accountability in this sector. This is important as intermediaries can certainly have an important function in transmitting information between shareholders and the company. However, the question of intermediaries is certainly one that will lead to some discussions – especially when it comes to the issue of the cost of the services they provide. There are some voices asking for those intermediary services to be free of charge. Certainly, there is once more the challenge of finding the right balance: On the one hand, a key feature of the proposals is to ensure that shareholders can actually exercise their rights – even across borders. That in turn implies that such activities must be doable in an affordable way. On the other hand, it cannot mean insisting on a free provision of such services.

As you can see, there are a couple of issues with the revision of the shareholder rights directive that will certainly inflict some debate. First in the Committee for Economic and Monetary Affairs, giving an opinion, and later on in the Legal Affairs Committee which is actually the responsible committee for this file. Personally, I find the overall direction of the

Commission's proposal to be encouraging. Strengthening and facilitating the overall level of shareholder engagement is laudable, if we do not want to end up in a system full of Alibaba-like companies. Now, is the time to have this discussion and to fight for improved shareholder rights as passionately as possible. Hence, I am very much looking forward to having this debate in the European Parliament. Thank you very much.