BDI
Bundesverband der Deutschen Industrie e.V.

Deutsches Aktieninstitut

POSITION

On the Draft revised Shareholder Right's Directive for triloge negociations

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The Federation of German Industries is the umbrella organisation of German industry and industry-related service providers. It speaks on behalf of 36 sector associations and represents over 100,000 large, medium-sized and small enterprises with more than eight million employees (www.bdi.eu).

Deutsches Aktieninstitut represents the entire German economy interested in the capital markets. Its about 200 members are listed corporations, banks, stock exchanges, investors and other important market participants. Deutsches Aktieninstitut keeps offices in Frankfurt am Main, Brussels and Berlin (www.dai.de).

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I. Introduction

The Federation of German Industries (BDI) and the Deutsches Aktieninstitut (DAI) welcome the work that has been done in order to find a compromise for the many neuralgic topics in the draft Shareholder Rights Directive. They would like to refer to some major points with this position. The articles 3 a-e are dealt with in a separate position paper.

The biggest impact on the German legal system would have had Article 9c in the version of the proposal of the EU Commission. Article 9c has thus been and still is the priority of the engagement of BDI and DAI with regard to the draft Shareholder Rights Directive. If the proposal had not undergone changes it would have had massive impact on German corporate group law and its allocation of responsibilities between the supervisory board, the management board and the shareholders meeting. As this probably was not intended the final compromise should reflect this. We also would like to refer to the strong link to the work on the acknowledgement of the so called "group interest" that has only started and which deals with related party transactions (RPTs) in the first place. **This work should not be foreclosed.**

Therefore it is of utmost importance that the proposal of the European Parliament to exempt transactions entered into between the company and one or more members of its group or joint ventures from the regime should be chosen.

BDI and DAI also welcome the proposed Member State options concerning the remuneration policy and report. A shareholder resolution legally binding the supervisory board in the dualistic systems means an (unnecessary) interference with its checks and balances. In that system neither the management board nor the supervisory board decide on their own remuneration: the supervisory board decides on the remuneration of the management board, the shareholders traditionally decide on the remuneration policy of the supervisory board which often is then even lead over into the companies' statutes. So, any conflict of interests are minimized while it is important for the supervisory board to keep the power over the Management Board's remuneration. Advisory "Say on Pays" have worked in the past, so resolutions with a low approval rate have led to changes in the remuneration systems even without legal compulsion.

Furthermore, BDI and DAI want to raise awareness to the fact that none of the Trilogue parties foresee a duty for proxy advisors to give issuers the opportunity to check the draft of the voting recommendation on its completeness and accuracy in a certain (short) period of time before its finalization in the context of Art. 3 i. Also, no general possibility for issuers to check voting recommendations before they are passed on to investors is granted. The granting of such a right would help to avoid significant legal and procedural problems on the side of the issuer affected.

Both federations want to repeat that it is of utmost importance to reject the position of the European Parliament on including rules on mandatory public Country-by-Country Reporting (CBCR) into the Shareholders Rights Directive.

It is necessary to wait for the outcome of the Commission's ongoing impact assessment and to address the issue in the context of the implementation of the OCDE BEPS rules on CBCR. Everything else would risk putting EU companies at a competitive disadvantage.

II. Detailed Comments

1) Article 9c: Related Party Transactions (RPTs)

BDI/DAI appreciate the proposed amendments to the EU Commission's proposal on the related party transactions regime. The EU Commission's proposal was much too broad and would have generated hundreds of votes on especially continental AGMs due to the corporate structures with concentrated ownership. It would not have been possible to make use of windows of opportunity anymore, companies would have been forced to reveal business sensitive information while their competitors outside of Europe are not obliged to do so. This would have had a negative impact on the competitiveness of European economy and would thus have challenged the objectives of creating jobs and growth as laid down in the Commission's agenda.

Now, a lot of the downfalls of the regime can be avoided by Member State options, like concerning transactions entered into in the ordinary course of business and concluded on normal market terms. It is principally acknowledged now that Member States like Germany can keep their corporate group law regime with its special checks and balances. **Within the trilogue negotiations it is therefore essential to maintain the already achieved improvements compared to the EU-Commission`s initial draft.**

But there is still more necessary to be achieved: the draft of the EU-Commission hasn't addressed accordingly transactions between the subsidiary and its parent company which is a typical situation that occurs in a corporate group. Transactions between the subsidiary and its parent company are exactly the situations where the special corporate group law regime installs minority protection prerequisites. Therefore, it is most important that the exemption rule of the Parliament is adopted whereas: "Member States may exclude from the requirements in paragraphs 1, 2 and 3: - transactions entered into between the company and one or more members of its group or joint ventures." **To only exempt transactions of the company with its subsidiaries is not enough**.

BDI/DAI would like to stress once more that Directive 2013/34/EU foresees transparency for related party transactions. These ex post disclosures have a preventive effect and should be considered as sufficient.

2) Article 9a: Remuneration Policy

DAI and BDI welcome the proposed Member State options by the Council and EP to provide that the vote by the general meeting on the remuneration policy may be advisory. The vote, however, should only be carried out on an ad hoc basis if a material change in the remuneration policy becomes necessary. Any automatism after three years as proposed by EP - without a system change before, creates unnecessary burdens on the preparation and holding of annual general meetings (AGM). The proposal of the council to hold an (advisory) vote in any case at least every five years, would still offer more flexibility than the three years option of the parliament.

Furthermore, the proposal is far too detailed and BDI and DAI do not see the need for detailed and binding rules concerning the composition of remuneration systems with regard to their design or content.

The EP proposal requires: "Member States shall ensure that the value of shares does not play a predominant role in the financial performance criteria. Member States shall ensure that share-based remuneration does not represent the most significant part of directors' variable remuneration." This provision should be deleted. It means an inappropriate intrusion into shareholder ownership rights to create longterm and sustainable incentives a share-based variable remuneration is the most used and appropriate system.

We are not aware that e.g. academic research has revealed that the requested content is in the best interests of the companies. A need for further restrictions has also not been justified in the proposal like it had been the case for the banking sector. Also, the alignment of shareholders' interests with management board incentives is very important to shareholders. So, shareholders want to see that the value of shares plays rather a significant role in remuneration systems. It would be a contradiction for the regulator on the one hand to give shareholders a "say on pay" and on the other hand prevent them from expressing their interests.

It should also be noted, that the proportion of the value of shares in the financial performance criteria actually cannot finally be calculated due to the volatility of share prices.

The parliament further suggests "that the policy shall indicate the appropriate relative proportion of the different components of fixed and variable remuneration." The word "appropriate" should be deleted, as only the existing status quo is reflected. The assessment, whether the proportion is appropriate takes place separately. The criteria for this assessment have been already defined at Member States level, e.g. in Germany in the Corporate Governance Code.

We are anyway of the opinion that it is the task of the supervisory board to responsibly balance the interests of shareholders and the company with its stakeholders by designing the remuneration policy. This also concerns the formulation on the "the role and functioning of the remuneration committee" in the parliaments resolution. In Germany the competent authority to deal with remuneration is the supervisory board. According to national law it is possible to establish a remuneration committee but it can only support with preparatory work, the decision has to be taken by the whole supervisory board. The according formulation of the council - committees concerned – is therefore the preferable option.

The suggestion of the parliament: "Where the policy is revised, it shall include an explanation of all significant changes and how it takes into account the votes and views of shareholders on the policy and report in at least the previous three consecutive years." should be deleted. It stays unclear, how the views of shareholders in a more or less "anonymous" AGM shall be collected.

As stated before in other documents of both BDI and DAI, in the dualistic system of a separate management and supervisory board it is important that the supervisory board has the full responsibility over the remuneration of the management board. Its authority and competence should not be undermined by a binding vote of the shareholders. The binding vote is not necessary, as practice has shown.

A negative or sometimes even a not overwhelmingly positive vote make the supervisory board rethink and redesign remuneration systems anyway. Additionally, shareholders can traditionally decide in the German system over the remuneration of the supervisory board bindingly. So, we believe that the current system works with its checks and balances.

3) Article 9b: Remuneration Report

Still, BDI and DAI recommend not to hold votes on the remuneration systems and additionally yearly on the reports even though, it is clarified that the vote on the report is advisory and even though the remuneration report is not more than the report on the application of a approved remuneration policy. Such provision leads to the danger of contradictory decisions by the annual general meeting – yes to the policy, no to the report – as majorities or shareholders might change. The supervisory board does not receive clear signals by such a vote and is left alone with the duty to take both into consideration.

The publication of the relative change of the remuneration of executive directors over the last three financial years, its relation to the development of the general performance of the company and the change in the average remuneration of employees over the same period, according to parliaments' resolution, will lead to a comparison between the companies. Given the various sectors, business strategies and developments, organizational or personnel structure (e.g. different personnel intensity, typical wage groups, national / international staff) a comparison between companies does not make sense or create any comparable figures and added value. Furthermore it will be difficult from to data protection reasons to collect data on the average remuneration of employees. What employees are covered (trainees, part-time employees, interns), all employees worldwide? What kind of remuneration is meant? Target remuneration or status quo-remuneration? This paragraph seems to be very problematic as regards its operationalization and validity. Please see also the discussions in U.S. on SEC-regulations concerning "pay ratio disclosure" (section 953(b) Dodd Frank-Act).

The parliament further favours a reporting obligation on the total remuneration awarded, paid or due split out by component, the relative proportion of fixed and variable remuneration, an explanation how the total remuneration is linked to long-term performance and information on how the financial and non-financial performance criteria where applied.

For the purposes of the financial performance criteria it should be noted that information on indicators for variable remuneration would allow direct conclusions about the budgeting behavior of companies. This is part of the essential internal corporate policy and disclosure may provide strategic advantages in particular to competitors. Therefore, we recommend that the information on the application of financial performance criteria is designed voluntarily.

The provisions on the report are already too detailed in the proposed directive, in our opinion. There should not be additional Delegated Acts concerning the remuneration report. When implementing the directive at a later stage, it should be kept in mind, to adapt the existing reporting obligations arising from national law, IFRS or Corporate Governance Codes. Different obligations would lead to different statistics on remuneration that could confuse shareholders instead of creating transparency.

BDI/DAI are concerned with the trend to foresee special (singular) provisions on liability and sanctions for boards into Directives and Regulations. Here, the Council proposes: "Member States shall ensure that the directors of the company, acting within the competences assigned to them by national law, have collective responsibility for ensuring that the remuneration report is drawn up and published in accordance with the requirements of this Directive. Member States shall ensure that their laws, regulations and administrative provisions on liability, at least towards the company, apply to the directors of the company for breach of the duties referred to in this paragraph."

First, this may interfere with Member States' jurisdictions and there is no justification for an EU harmonisation. Second, such special provision on liability does not reflect the meaning of the remuneration report to shareholders.

While the compliance with other management and supervisory board duties may have a much more significant impact on shareholders or the company there are no equal sanctions in the EU stipulated in this or other Directives.

4) Article 3i – Proxy Advisors:

BDI and DAI generally welcome the idea of more transparency in the proxy advisor industry. However, one of the most important topics from the issuers' point of view is not addressed by any of the three parties: A duty to give issuers the opportunity to check the draft of the voting recommendation on its completeness and accuracy in a certain (short) period of time before its finalisation. Only such a duty ensures, that factual errors are discovered and can be corrected by the proxy advisor. In case of dissent on a particular voting recommendation the proxy advisor should ideally also pass the dissenting opinion of the issuer together with the PA's voting recommendations to the investors.

Proxy Advisors should further be obliged to take "company-specific circumstances" into consideration, when drafting their recommendations. This would prevent proxy advisors from applying their worldwide guidelines on all companies uniformly and recommend voting at AGMs that would interfere with the companies' corporate policy.

A general possibility for issuers to check voting recommendations before they are passed on to investors would be very helpful to avoid the publication and dissemination of formal mistakes. These formal mistakes can cause significant legal and procedural problems on the side of the issuer affected, especially if they lead to negative voting recommendations. These kind of problems could easily be avoided if the issuers got the opportunity to fact check the recommendation.

Furthermore, we favour the idea of the EP and the Council with regard to a duty of the PA to disclose „the essential features of [the research undertaken and - EP] voting policies applied for each market" (Art. 3i 2. ca). Issuers can take them then into account by setting up the agenda for the annual general meeting.

We also welcome the proposal of the Council in Art. 3i 4a; this Article applies to proxy advisors having their registered office or head office outside the Union which carry out their activities through an establishment located in the Union. Otherwise proxy advisors located outside the EU would have advantages against their European competitors.