

Inspired thinking



Progress in cross-border voting in Europe

With thanks to Eugenia Jackson, of Manifest, the guest author of this article.

This article should be read in conjunction with “The prospects of cross-border voting in Europe”, which was written by Paul Hewitt of Manifest and published by Insight in August 2006, which outlines impediments to cross-border voting.¹

Introduction

Greater international ownership of European public companies has highlighted the importance of establishing good systems to allow easy and reliable cross-border voting. In recent years, The European Commission has put significant effort into identifying barriers to effective voting in EU member states and finding ways to make improvements. This resulted in the Shareholders’ Rights Directive, which was approved by the European Parliament in February 2007. We believe the Shareholders’ Rights Directive covers a number of important issues aimed at simplifying the voting process, however, there are systemic issues that have not been addressed by the Directive.

Shareholder Rights Directive

The Shareholder Rights Directive is intended to set minimum transparency standards for companies incorporated in the EU whose shares are traded on a regulated market such as the London Stock Exchange. It aims to ensure shareholders in member states may vote without difficulty at company meetings. Its key proposals include those relating to the provision of sufficient advance notice for meetings, the removal of legal obstacles to electronic participation and the ability to vote without attending the meeting.

Manifest Research

Manifest recently released a study of the practical problems of voting in 18 key European markets to assess what additional changes to the Directive might be needed. In addition to reviewing local market procedures, Manifest also asked key investors to rank their concerns. Three key sets of issues were raised:

1) Market issues

There are two specific market issues that we would like to address. The first issue is the time fund managers need to make informed voting decisions. Our research suggests that this can vary from 48 hours to two weeks, or longer if there are any controversial issues to address or if engagement with the company is necessary to discuss and resolve them. In practice, the time available to make the decision on the vote varies significantly. Manifest’s research showed that in 10 out of 18 markets, investors simply do not have enough time to think carefully about votes. This tends to lead to them taking a ‘box-ticking’ approach and issuing standing instructions, often to vote with management or simply follow voting agency recommendations, which does not lead to an informed voting decision.

The second market issue is that each company usually has one or sometimes two shareholder meetings each year. This means that the typical institutional investor has to deal with over 3,000 meetings and tens of thousands of proxy votes.

¹ See http://www.insightinvestment.com/uk/responsibleinvestment/riandcg/ri/literature/ri_literature_archive/.

Although the UK proxy season stretches from March to June, European issuers tend to concentrate their meetings into just one week, leading to a 'Europe Day' phenomenon on the last Thursday in April. This approach creates a terrible logistical bottleneck for all involved and should be reviewed.

2) Problems at the issuer level

Many European companies still issue 'bearer' shares. If an investor holds bearer shares, their shareholder status has to be confirmed by the local custodian bank, that holds the assets in an account, which certifies to the company, when requested, that the shares are in the account. Bearer shares restrict investors' ability to trade, as the shares must remain in the bank in which they are deposited (i.e. they are 'blocked'). The practice of 'shareblocking' requires investors either not to exercise their voting rights or to surrender the right to dispose of their shares for a defined period of time.

3) Inefficiencies caused by the complex "chain of intermediaries"

Voting in Europe involves a so-called chain of securities intermediaries which involves on average seven separate stages from issuer to the voting decision maker (e.g. issuer – tabulator – sub-custodian – global custodians – voting service provider – fund manager or beneficial owner). Meeting information and instructions are pushed up and down the chain between the issuer and the voting decision maker, which takes a great deal of time. It causes unnecessarily early voting deadlines for the decision maker because it takes so long for the instruction to pass back up the chain. In addition, a significant number of votes are lost due to the wide use of pooled accounts by securities intermediaries and the lack of audit trails.

The long chain of intermediaries also increases the operational risk that somebody might make a mistake in the process, as the sheer number of agents involved increases. This also greatly hampers the ability to audit voting, because an audit trail (like a voting process) is only ever as strong as the weakest link in the chain.

Solutions

It was widely agreed among the study group that cross-border voting would be much simpler if issuers could agree to voluntarily adopt uniform standards on meeting notification periods, record dates and voting deadlines. Specifically, they suggested that voting deadline dates should be set to two to four days before the meeting so that investors and analysts alike can benefit from greater certainty regarding the timescales to which they are working. This would facilitate a much more consistent approach to analysing meeting business, thereby improving the quality of decision-making and the understanding of meeting issues.

Companies should recognise that it is impossible for institutional investors to be physically present at all shareholder meetings, and they need, instead, an efficient remote voting process. Ideally, shareholders would like all relevant materials (including translations) to be made available 30 days before the Annual General Meeting, with all material put on the company website and an option to receive a hard copy.

Finally, institutional investors would benefit greatly if company meetings were spread out more evenly over the proxy season.

Conclusions

Manifest believes that the Shareholders Rights Directive is a significant step forward, but it does not solve every problem related to cross-border voting. We believe the voting process could be far more efficient if investors were able to send votes directly to tabulators through their preferred electronic voting platform and bypass unnecessary intermediaries in the chain. This is the approach that the US Securities and Exchange Commission has recently taken and is the approach that the UK and Ireland have successfully operated within for many years.

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