

Inspired thinking



The prospects of cross-border voting in Europe

With thanks to Paul Hewitt, Business Development Manager, Europe, at Manifest, the guest author of this article.

Introduction

In the 21st century world of wireless communication technology, chip and pin and online banking and payments, you could be forgiven for thinking that shareholder voting across borders might be straightforward. You would probably expect that the counterparties with responsibility for trillions of pounds of assets between them would have highly efficient systems that enable the seamless, equal treatment of shareholders wishing to send voting instructions to a meeting.

Impediments to cross-border voting

Unfortunately, this is not the case. Such systems do not exist, but it is not technology that's the critical impediment to investors exercising their right to vote. In fact, no two European legal systems are exactly the same when it comes to shareholders' rights, thus every country is unique in its approach to voting.

The legal systems vary in four principal ways:

- the method by which shareholders are identified as such by the issuer;
- the manner in which shareholders are informed about meetings;
- the methods by which shareholders are able to cast their votes, and;
- the rights that shareholders are entitled to exercise at meetings.

Identification of shareholders

In the UK, we have an electronic registered share system that makes it easy to compile a shareholder register to identify who holds the entitlements to voting rights. These registers are continually updated. However, in many European countries, share registers are not necessarily maintained in the same way, nor are shares always registered. This means that the system for identifying who has the right to vote is much more cumbersome.

For instance, if an investor holds bearer shares, their shareholder status has to be confirmed by a local custodian bank, who holds the assets in an account and then certifies to the company, when requested, that the shares are in the account. A guarantee of this certification requires that these shares must remain with the bank at which they are deposited, meaning they cannot be traded i.e. they are 'blocked'. For many investors, the relative risk of having shares blocked outweighs that associated with not voting – so they don't vote. Blocking is prevalent in a number of countries, including Belgium, Greece and Italy and is possible in many others.

Notification of meetings

Shareholders are also not given uniform access to information about an upcoming meeting across Europe. Italian companies do not publish the annual report until after the AGM has approved it and resolutions are not always listed as distinct from agenda items. However, the most critical impediment is the notice period given to shareholders of a forthcoming meeting. This ranges from 42 days in Germany to little more than a week in Denmark. In some cases, shareholders may not know

about a meeting until after it is too late to do anything about it. This is not only to do with the short notice at which meetings may be called in some countries, but also to do with the time it takes for notifications and documents to reach the shareholder through the chain of intermediary banks. Sometimes notifications and voting instructions have to pass along a chain with three, four or even five intermediaries.

Voting systems

Even if it has been possible to identify a shareholder and an investor has got hold of enough information with enough time to make an informed voting decision, the investor's ability to express their choice may be curtailed by another set of impediments, such as their legal right to representation at the meeting if they are not able to attend and the method by which the investor's votes are sent and cast. Most Scandinavian companies require shareholders or their representative to be physically present at the meeting in order to cast votes. Investors may also be limited in their choice of who their representative is; they may have to be a relation, another shareholder or an independent representative appointed by the company, rather than someone of the investor's choice.

Further, even if remote voting ahead of the meeting is permitted, electronic voting is by no means guaranteed. For example, although electronic voting was enabled over four years ago in France, most French companies still insist on a paper ballot form with signatures. Paper-based postal voting is a cumbersome process; some require signatures and that the form passes through a number of different entities on its way through the process, which may already be severely time-constrained.

Voting rights

Lastly, the voting rights attached to a share may not be commensurate with the economic interest in the company it represents. In simple terms, the voting power may not be proportionate to the amount of money invested in the company. Many Scandinavian companies are characterised by controlling shareholders who hold shares with disproportionately large voting rights (shares whose voting rights may be ten times greater than those attached to other shares in the company). Shareholders in French companies

may find themselves given additional voting rights at no additional investment cost simply because they have held shares for a given period of time. This has the effect of partially disenfranchising other shareholders.

There may also be requirements for a shareholder (or group of shareholders) to hold a minimum number of shares before they even have a right to vote – as is often the case in Spain, Portugal, Switzerland and Norway. Such requirements discriminate against small shareholders and foreign shareholders.

Potential solutions

Thus far, the picture looks gloomy. However, there is light at the end of the tunnel, both from a regulatory and practical perspective.

European issuers are becoming more forthcoming in making information available to investors. Often, company websites offer a wealth of information of importance to shareholders, such as meeting announcements, annual and financial reports, contact names, governance structures and so forth. Shareholders can therefore be made aware that a meeting is to take place in good time, provided, of course, that they regularly track the website, or rely on someone to track it for them.

Increasing awareness of the importance of voting (driven in part by regulatory requirements in some countries and in part by the increasingly high profile company meetings are receiving) means that the seriousness of the problems set out above has begun to be recognised, which has led to demands for the European Union (EU) to act.

A report commissioned by the EU from a specially formed High Level Group of Company Law Experts (the 'Winter Report', after Jaap Winter, the Chairman), identified many of these problems, which are now the subject of a proposal for a Directive by the European Commission on Shareholders Rights. For example, under the proposed Directive, pre-meeting notice periods will be subject to a statutory minimum of 30 days across Europe, so that investors in all EU member countries will know when meeting materials are available and will be notified of meetings.

The Directive also proposes to do away with share blocking, which would effectively mean the conversion

of all bearer shares to registered shares, along with a universal move to a system that establishes who has the right to vote, within a limited time period. The right of shareholders to be represented by whomever they wish is also under consideration, along with the abolition of rules relating to minimum shareholding thresholds, enabling much more flexibility for shareholders to ensure their shares are voted.

Perhaps most significant, in terms of goals set out by the Shareholder Rights Directive, is the desire to encourage companies to use electronic voting, taking advantage of new technologies for remote simultaneous voting and electronic voting ahead of the meeting, which were simply not available when Member State laws were drawn up.

(In addition, European countries are also looking independently at reforming their own systems: just this year, Sweden strengthened the implementation and provisions of its code of corporate governance (including provisions for allowing voting in absentia); Luxembourg now has a Corporate Governance Code; and Belgium has passed a law to get rid of bearer shares by the end of 2007.)

It is hoped that the European Shareholder Rights Directive will be agreed by Member States in early 2007, with implementation completed by the end of 2009. We believe that the measures proposed should engender investor confidence in the voting process and thus encourage more investors to vote.

Regulation isn't the only answer

In the meantime, there is still room, and arguably a forceful business imperative, for the counterparties – intermediaries, issuers and shareholders – to make voting easier by improving the transparency and the quality of communication of voting instructions. Specifically, there is a need to dismantle arbitrary restrictions and over-bureaucratic processes in place

at present, and make the most of today's technology. (The current project to update the SWIFT voting message types is a good example of the potential the market has to create and define new standards that enable processes to be improved.)

Conclusion

Although European voting looks set to become easier as the reform process gathers momentum we should not be complacent: there is still a very long way to go. Many laws have yet to be radically changed, both at the national and company level before the current system becomes more user-friendly.

Moreover, attitudes and processes need to be redefined to take advantage of legal changes, not least of which would be the de-coupling of the voting instruction process from the registration and notification processes, allowing more flexible, innovative voting solutions to be put in place. In order for market-led solutions of that nature to emerge, such as the direct electronic UK voting in place at Manifest, regulators (including stock exchanges, Financial Regulatory Authorities, securities depositaries and even custodian banks) need to allow the market to breathe by setting standards, not processes.

The development of a more workable European market in cross-border voting should generate several benefits for investors and companies alike. It should reduce discrimination faced by small and non-national shareholders; it should reduce the cost and resources that shareholders have to invest in voting; it should make investing in European companies more attractive; and it should ease the flow of capital around Europe by reducing the risks previously inherent in having an economic interest in a company, but not the appropriate commensurate control. All in all, it should significantly improve the working and efficiency of European share markets.

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