EALIC
European Association of Listed Companies AISBL-IVZW

EALIC'S Reply
to
CESR'S Call for Evidence on the Possible CESR Level three Work on the Transparency Directive
Ref. : 07-487

14.09.07

EALIC would like to reply hereinafter to CESR's call for evidence dated 13 July 2007 regarding possible level three measures by CESR concerning the Transparency Directives. EALIC understands that CESR is looking for evidence on the areas in which measures should be adopted with a view to ensure the consistent application of the Transparency Directives in all Member States. At this stage CESR is looking at these areas where different national practices would result from an inconsistent application by Member States rather then from legitimate national discretions. In addition, CESR is also solliciting the stakeholders' input in view of the creation of the EU network of national storage mechanisms.

1. Do you consider that CESR should start working in its Level 3 capacity in order to promote aconsistent application of the Transparency Directive and the Level 2 Directive?

EALIC agrees with CESR that the risk of inconsistent application of the Transparency Directives at national level is real and therefore strongly supports CESR level three coordination work in order to manage the same. The regrettable effects of the inconsistent application of harmonised measures may be seen in the prospectus area: in its recent report on the supervisory functioning of the Prospectus Directive and Regulation (Ref: CESR/07-225), CESR points out that market participants' main concerns are not focused on the European legislation on prospectus as such but on the divergent practices of the different competent authorities that they identified in a number of areas. As in the Prospectus area, an inconsistent approach at CESR's members' level could hamper the proper functioning of the harmonised provisions set forth by the Transparency Directives and impede the achievement of their fundamental goal to increase investor protection and market efficiency at a pan-European level.

2. If yes, which areas do you think CESR's work should cover? Could you prioritise them?

EALIC concurs with the areas for action as proposed by CESR and in particular with the following:

a) The application of the notification of holdings regime in general

EALIC believes that CESR should give priority to the area concerning the application of the notification of holdings regime. The provisions contained in the Transparency Directive and in

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the Level 2 Directive prove to be complex and difficult to adhere to in practice because of the number of uncertainties raised by the nature of the holdings that are concerned by the disclosure requirement, the thresholds at which holdings are required to be disclosed, the operational problems associated with the reporting of major holdings and the time period in which a shareholder has to make the disclosure and to whom. CESR should seek to clarify such aspects and to provide practical guidance and build further on its Final Technical Advice of June 2005 (see ref: CESR/05-407), hereinafter "CESR's June 2005 Advice".

In addition, EALIC would encourage CESR to strive for a uniform approach throughout the Community as regards the provisions concerning the thresholds and the timeframe for reporting, despite their minimum harmonization nature, because this would render cross-border investments and transactions possible without extra administration and monitoring costs for investors. The flexibility that is currently left to Member States and to companies in the area of thresholds seems to cause great concern to, among others, institutional investors who operate on a cross-border basis and have great difficulty to comply with the many diverse applicable regimes. The consequence is that the transparency provisions may not be applied in an accurate manner or not applied at all. In the same sense, a uniform approach as to the regime of sanctions applicable in case of non-compliance, would certainly render the Transparency legislation more efficient.

As a side note, although of key importance for issuers, EALIC would like to draw CESR's attention to the crusade that issuers have been undertaking the last couple of years to have a legal framework that would allow for real shareholder transparency for all shareholdings large and small and such on a permanent basis independent of the reaching, exceeding of or falling below any thresholds. Issuers have not ceased pleading with the European legislator to lay down such a regime, but the latter seems to believe that the Transparency Directives should offer a satisfactory level of transparency, *quod non in casu.* EALIC takes the liberty to attach hereto the position paper dated 23 July 2007 it has lodged with the Commission in reply to its Third Consultation on Shareholders Rights (See notably III.1 Duties of intermediaries and III.2 Disclosure of investors with EALIC's arguments why more transparency is needed and why the Transparency Directives are not sufficient in this respect).

b) Application of the notification of holding regimes to stock lending and to derivative products.

EALIC has consistently requested more transparency in the area of stock lending. In its reply to the Commission's Third Consultation as cited above, EALIC advocates complete transparency towards all concerned parties, including the issuer (See II. Stock lending). EALIC recommends that there should be no stock lending without the shareholder's explicit consent and recommends to put a regime in place to safeguard the shareholder's rights, including and especially the right to vote and the right to control this voting right at all times. To increase the transparency EALIC recommends for instance: "*The lender should inform the issuer of stock lending agreements that result in a holding of stock representing 1 % or more of the voting rights, in a period running as of 15 days before the record date up to the date of the general meeting, disclose the identity of the shareholder and of the borrower."* In addition EALIC recommend that "*Institutional investors should clearly disclose their policy with regard to stock lending."* Finally EALIC thinks that

these provisions should also apply to practices similar to stock lending insofar they imply a temporary transfer of voting rights.

Article 10 (b) of the Transparency Directive extends the notification obligation of major holdings to a natural or a legal entity that is entitled to acquire, to dispose of, or to exercise voting rights in case of voting rights held by a third party under an agreement concluded for the temporary transfer for consideration of the voting rights. In CESR's June 2005 Advice, CESR doesn't state whether stock lending would or could constitute such temporary transfer for consideration of the voting rights. It is important to have clarity on this question.

Clarity is also needed as to whether and to what extent article 10 and article 13 cover situations typically characterized by the separation of voting rights (i.e. the right to vote shares under company law) from economic ownership (i.e. the economic returns associated with the share). The economic ownership of the share is often combined with coupled assets including derivatives (such as options, futures and equity swaps) as well as contractual rights (such as rights under a stock lending agreement). Does art. 10 concern shares and the voting rights attached as mentioned in CESR's June 2005 advice (nr. 129) that says that both shares and voting rights are covered? Or does art. 10 cover (also) the situation where the voting right would be separated from the economic right? Art. 10 g) concerns the situation where the shares are held by a third party in his own name although the voting rights are controlled by the actual shareholder, for instance in case of a trust (see CESR June 2005 advice nr. 169). What about the opposite situation in which the third party (apparently) controls the voting right and the shareholder has the economic right? The same question arises for article 13 that refers to shares to which voting rights are attached, already issued. EALIC believes that for many financial instruments, in particular derivatives the Transparency Directive disclosure requirements might not apply. Would CESR support an extension of the scope of the major holdings disclosure provisions to the above mentioned security interests? A coordinated application of the Transparency provisions and the existing Market Abuse provisions might be useful in this respect. The disclosure of situations excluded from the Transparency Directive could indeed be reached through the Market Abuse provisions.[1]

c) Application of the information requirements for issuers as described in articles 16 to 18 of the Transparency Directive.

Articles 16 to 18 of the Transparency Directive contain provisions about communication requirements to and from shareholders as well as timely access to information. Articles 17 and 18 require that Member States ensure equal treatment for holders of shares and/or debt securities who are in the same position and that all information necessary for shareholders to exercise their voting rights be available in the home Member State. Equal treatment, according to recital 22, does not prejudice the issue of how many voting rights are attached to a particular share. Furthermore, holders of shares and/or debt securities situated abroad should be more actively involved in that they should be able to appoint proxies to act on their behalf. Articles 17 and 18

[1] For instance, if a swap linked to the issuer's shares is carried out on his own account by a person discharging managerial responsibilities within the issuer, the transaction shall be disclosed to the public (see article 6.4. of Directive 2003/6/EC). Unlike the Transparency Directive, these provisions concentrate on the economic ownership of the shares rather than on the voting rights.

further call on the Commission to adopt, whenever required, implementing measures to ensure, *inter alia*, the uniform application of these principles.

EALIC agrees that further work on access and dissemination requirements should be consistent with already enacted legislation, including the recently adopted Directive on the exercise of certain rights of shareholders in listed companies.

d) Application in practice of the standard forms for notification of holdings

CESR should indeed also monitor the application at national level of the standard forms for notification of holdings and adopt appropriate measures against its members which would not promote a full adherence to the standard.

3. Do you think CESR's work to harmonise should be published in the form of a Q&A section of its website (in a similar way as CESR is currently doing in the prospectus area)?

In EALIC's opinion, the Q&A is a valid and flexible means of reducing the divergent practices in Member States. However, this should remain supplementary to and not replace CESR's other coordination activities at level three.

4. Do you think CESR should facilitate the establishment of an EU network of national storage mechanisms?

EALIC agrees that CESR could play a role in assessing progress towards the creation of a European network of storage mechanisms.

Article 22 of the Transparency Directive calls on Member States to draw up guidelines in view of facilitating public access to financial information. The aim of the guidelines should be the creation of two layers of electronic networks: one at national level linking the storage mechanism(s) to the business registries and another one at European level linking national systems. The latter's aim would be to provide a one stop shop to investors when looking for regulated financial information. Article 22 further calls on the Commission to review the results achieved under these Guidelines and provides it with the necessary authority to adopt, whenever required, implementing measures.

The competent authorities of Member States have not yet drawn up national guidelines pursuant to article 22. However, they have expressed their preference, via CESR's advice of June 2006, for the so called model C of the European network. Under model C, the EU network would be accessed via a common interface which would contain a list of all EU listed companies. The user would be directed to the site of the relevant storage mechanisms. The data would remain at national level and the only common element would be the list of companies.

In a working document dated March 2007, the Commission services are proposing the minimum conditions that a pan-European network of national storage mechanisms operating under Model

C should meet. These conditions relate to the institutional and technical interoperability elements of the agreements that storage mechanism should conclude among themselves, as well as to the pricing of access to information (access to information stored in the mechanism in its raw format should be free of charge to investors).

EALIC has pleaded in favour of separating the storage of regulated information which is a public good and should be better performed by a public infrastructure, from the added value services based on this raw information which should be left to profit oriented companies operating in a competitive environment.

Therefore, EALIC agrees that, before implementing measures are adopted, further work is needed to assess how these governance and pricing principles would apply, with a view to ensuring a smooth operation of the network.

In addition, with regard to the specific model of an EU network of national storage mechanisms EALIC would disagree with the proposal to use the BRITE project as common interface under Model C. The establishment of the European network of central storage mechanisms at the level of European Business Registries could give rise to a concentration in the form of a substantial monopoly and any abuse of this monopoly would violate the fundamental principle of free competition established by the EC Treaty.

Although the publicity duties performed by the national business registries are certainly in line with EU provisions as they are set forth in the First Directive (First Council Directive 68/151/EEC of 9 March 1968), it cannot be ignored that the disclosure regime provided for by this Directive needs to be updated following the technological developments of the last decades.

Moreover, with reference to the funding and pricing of access to information, it should be considered that notwithstanding the public nature of the disclosure services to be provided by the national business registries pursuant to the First Directive, they act as profit-making entities and do not perfectly adhere to the provision of article 3, paragraph 3 of the First Directive which imposes them to charge a price not exceeding the administrative cost for the copies of corporate documents. Such a provision should in any case be taken into account when determining the funding and pricing under the pan-European network of central storage mechanisms.

Enclosure: EALIC's Reply to the Commission's Third Consultation on Shareholders Rights

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EALIC'S REPLY
TO
FOSTERING AN APPROPRIATE REGIME FOR SHAREHOLDERS' RIGHTS

Third Consultation Document
MARKT/30.04.2007

23 July 2007

EALIC welcomes the initiative taken by the Commission to launch a consultation regarding a possible Recommendation with a view of complementing the Directive of the European Parliament and of the Council on the exercise of certain rights of shareholders in listed companies, hereinafter the "Shareholder Rights Directive". European issuers believe indeed that such recommendation would be necessary to reach the objective, namely remove the barriers to a smooth, timely and cost efficient cross border exercise of essential shareholder rights, including the right to participate and vote at general meetings. Shareholder rights are a very important topic for listed companies and EALIC wishes therefore to make a constructive contribution to the debate. Hereinafter are EALIC's comments on the Commission's proposals as well as amendments thereto.

I. LANGUAGE OF MEETING DOCUMENTS

Question 1:

Q 1.1.: Do you think there is a need for action in that area?
Q 1.2.: If your answer is yes, do you think a recommendation along the following lines would go into the right direction?

"1. Companies should make available to their shareholders the convocation for a general meeting, the meeting agenda and the documents to be submitted to the general meeting at least also in a language customary in the sphere of international finance, unless the General Meeting decides to the contrary.
2. Point 1 should not apply to companies
- that fulfill at least two of the criteria established by Article 11 of the Fourth Company law Directive on annual accounts (not exceeding a balance sheet total of EUR 3 650 000, a net turnover of EUR 7 300 000 and an average number of employees during the financial year of 50), or
- that neither have a wide foreign shareholder base (on average under 10% of the subscribed capital) nor are actively seeking foreign investment.
For these companies, the obligation referred to in point 1 should only apply where this is requested by shareholders representing at least 1/3 of the subscribed capital."

EALIC believes that companies with a known foreign shareholder base will naturally want to make relevant documentation available in a language that can be understood by

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the largest possible number of shareholders. Being able to enter into a dialogue with their shareholder base is indeed of prime importance to listed companies.

However, when recommending the use of an additional language, such as a language "*customary in the sphere of international finance",* the Commission should carefully **consider the scope of documents** it would subject to such translation recommendation. The fact that a given language would be accessible by a large population is not the only consideration to be taken into account. Equally important is the efficient allocation of resources. As a consequence, one should bear in mind that in contrast to the notice and the agenda that are usually pretty straightforward, both the resolutions and the underlying documentation can sometimes consist of many hundreds of pages drafted in very complex and specific technical jargon. This is for instance the case when the general meeting has to decide on a merger or acquisition. While we agree that ideally the resolutions and supporting documentation are best included in the translation, we believe that **management would be best placed to judge** on the necessity and desirability to do so depending on the circumstances of the case.

Moreover it should not be forgotten that the set of documents related to general meetings can undergo changes during the process due to a shareholder exercising his right to add items to the agenda or table additional resolutions. In the same sense, it can also happen that a general meeting is being called at the initiative of shareholders. These situations should be reflected in the **allocation of the costs** of translation.

EALIC **concurs with the principle laid down in paragraph 2**, namely that the companies indicated therein should not be under any external pressure whatsoever to provide for a translation of the concerned documents. However EALIC believes that the threshold should be **raised to 15 %** and that it would make more sense to work with 1/3 of the voting rights instead of 1/3 of the subscribed capital**.** The Recommendation should also provide that the concerned company be given a reasonable delay for the translation. Finally we would like to stress that we must not forget that we are dealing with a recommendation here. Therefore the word "obligation" used in the concerned provision must be replaced as it doesn't fit with the purpose of a recommendation which is per definition not binding.

The Commission proposal is based on the assumption that companies issue general meeting related documents in their home language, hence the proposal to make them available in an *additional* language. EALIC considers that Member States should have the possibility to leave the companies free to use any language they may deem fit taking into account their shareholder base. As a consequence, Member States could then enable companies to use "*a language customary in the sphere of international finance"* such as English either **"*in addition to*" or "*instead of*"** the official language(s) of the Member State in which the company is incorporated. The Commission should make this recommendation to the Member States so that they create the right legal framework thereto.

Finally, the Recommendation should also state clear that in case of diverging language versions, the text drafted in the original language should prevail.

The Recommendation should therefore read [1]***:***

"1. Companies ***with a known large foreign shareholder base*** *should make available to their shareholders the convocation for a general meeting* ***and*** *the meeting agenda at least also in a language customary in the sphere of international finance, unless the General Meeting decides to the contrary,* ***and should be encouraged to do so at the discretion of the management for the draft resolutions and the supporting documents to be submitted to the general meeting.***
2. Point 1 should not apply to companies
- that fulfill at least two of the criteria established by Article 11 of the Fourth Company law Directive on annual accounts (not exceeding a balance sheet total of EUR 3 650 000, a net turnover of EUR 7 300 000 and an average number of employees during the financial year of 50), or
- that neither have a wide foreign shareholder base (on average under ~~*10*~~***15*** *% of the subscribed capital) nor are actively seeking foreign investment.*
For these companies, the ~~*obligation referred to*~~ ***provision*** *in point 1 should only apply where this is requested by shareholders representing at least 1/3 of the* ~~*subscribed capital*~~ ***voting rights and provided such request is made in a timely manner to allow companies to comply.****"*
3. In the event where the documents mentioned under point 1 undergo changes due to the exercise of the right of a shareholder to put items on the agenda or table draft resolutions, the costs related to the use of an additional language should be borne by the concerned shareholder. The same should apply when a general meeting is convened at the initiative of a shareholder.
4. As an alternative to the use of an additional language mentioned under point 1, Member States should consider to allow companies meant there under to use a language customary in the sphere of international finance either in addition to or instead of the language of the Member State where the company is incorporated, unless the General Meeting decides to the contrary.
5. In case of divergence between the original version and the translated version, the former will prevail.*"*

II. STOCK LENDING

Question 3:

Q 3.1: Do you believe that stock lending needs to be addressed at EU level? Please give your reasons.
Q 3.2: If your answer is yes, would you support recommendations along the following lines?

[1] Deletions in strike through; additions in bold.

"1. Stock lending agreements should contain provisions informing the relevant parties of the effect of the agreement with regard to the voting rights attaching to the transferred shares.
2. Member States should ensure that shares can only be lent by financial intermediaries where the investor has explicitly agreed to his shares being used for stock lending in the framework agreement with his financial intermediary.
3. Borrowed shares should not be voted, except where the voting rights are exercised on instructions from the lender.
4. Stock lending agreements should provide that borrowers have to return equivalent shares to those borrowed promptly upon the lender's request."

EALIC agrees that the issue of stock lending should indeed be addressed at **EU level**, because this seems the only way to clear the legal and practical chaos which is currently surrounding this business. It is of utmost importance to bear in mind the peculiarities of the economic and legal context described hereinafter, when contemplating how the issue could be efficiently addressed at EU level. Having said that, we do not wish to propagate strong community measures. We rather believe that a recommendation or the adoption of best practices codes would be appropriate.

Economic context of stock lending

EALIC acknowledges the importance that the practice of stock lending has taken over the last years as a financial product and recognises also the benefit it can bring to financial markets by increasing their liquidity. EALIC does not wish therefore to put into question the practice of stock lending as such. However, issuers are much concerned about the possible side effects of stock lending on the running of their companies in general and on the functioning and outcome of their general meetings in particular.

Stock lending can be done for a number of reasons, some of them lying with the investor while others are lying with the financial intermediary holding the securities in custody or having to manage the securities portfolio under an asset management contract. Sometimes, the reason is simply **financial speculation**, the borrower speculating to be able to sell, at his turn, the shares at a higher or equal price and return shares bought at a lower price to the lender. An important reason for financial intermediaries to engage in stock lending is to **cover positions resulting from short selling**. In today's global markets, intermediaries are involved in financial and securities transactions that go around the clock and around the globe and which volume and importance can only be described in dazzling figures. It has become routine business to back these operations with lent or borrowed securities. Although it seems to have become less frequent, stock lending is often also inspired by **dividend payment reasons**. It can indeed be observed that in several countries stock lending activities radically rise at times of companies' general meetings, often to allow borrowers to benefit from cash distributions (dividends) or lenders to avoid taxes on dividends.

Risks

Unfortunately, there have been reports of stock lending where securities are borrowed for the unique purpose of influencing the outcome of general meetings or even of taking control of a company with a **short term view focusing on purely personal financial gain at the detriment of the company's longer term interests as an enterprise**.

In Europe many financial institutions claim that they usually refrain from exercising the voting rights attaching to borrowed stock. However, in those cases the problem is that the stock is not voted at all. This situation is again not harmless because it is in the interest of companies and their shareholders that the latter do express themselves at general meetings. Otherwise there is a real risk that at the general meetings decisions are being taken by an incidental majority that might not always be inspired by the company's best interest (see hereinafter "2. Disclosure of investors").

It has been reported that in the USA, intermediaries do not keep track of what shares are being lent in view of exercising voting rights, the unfortunate consequence being that serious cases of over-voting or double voting have already taken place.

Legal context of stock lending

Most of the current concerns stem from a lack of legal certainty or at least legal awareness: the market has no clue about the rights and obligations arising from stock lending for the parties involved in or concerned by the transaction. There is also a wide spread concern for a possible abuse of such rights and obligations by parties who wish to exercise influence on a company's affairs in an illicit manner. How could it have come so far? The answer is that although stock lending is widely practised in financial markets across the globe, there is **no uniform legal approach let alone a minimum of common legal framework**. The truth is that stock lending transactions appear to be exclusively governed by private contracts. Most, if maybe not all, national legislation even seems to remain silent on the subject.

The uncertainty extends to the **very basics** of the practice of stock lending: there is not even clarity on some of the core aspects: does stock lending legally qualify as a loan or rather as a sale and buy-back transaction? Is the lender the shareholder or a financial intermediary like a custodian? Does stock lending involve a transfer of ownership and if so, what happens with the inherent corporate and economic rights? In most cases and in spite of its name, stock lending seems to be constructed as a sale and buy-back of the concerned shares. As a consequence, the transaction implies indeed a **transfer of ownership of the securities and, as a result thereof, of voting rights** attached to the securities from the lender to the borrower. A serious problem therefore arises where the lender is not the shareholder - and therefore not the owner of the shares - and acts without the knowledge, let alone the agreement, of the shareholder. The matter becomes even worse when we realise that since the entire transaction and its side effects are the exclusive subject matter of private covenants, the market, not in the least the issuer but also other shareholders, will not necessarily be aware of what is happening.

True, the Transparency Directive extends the notification obligations of the acquisition or disposal of major holdings it lays down for shareholders, to a natural person or legal

entity that is entitled to acquire, to dispose of, or to exercise voting rights in case of voting rights held under an agreement concluded for the **temporary transfer for consideration of the voting rights**[2]. Insofar this provision would cover the case of stock lending, notification would have to be done of such information as the resulting situation in terms of voting rights, the identity of the shareholder, etc.[3]. It remains to be seen however what effect this provision will have in practice. At any rate, as is the case with the disclosure of shareholders in general (see hereinafter), transparency would only be required for very large transactions and only in case the thresholds are (not any longer) exceeded. EALIC believes that such is far from satisfactory as it does not acknowledge the legitimate request of issuing companies to know its shareholders (or in this case, the persons holding the voting rights) (see hereinafter).

Finally, the Commission should not limit the scope of its recommendations to enhance transparency to transactions of stock lending but should extend it to similar mechanisms implying a temporary transfer of voting rights.

EALIC's recommendations on stock lending

Considering the above, EALIC strongly believes that the basic principles should be straightened out first and made crystal clear to the market so that all stakeholders are able to assess the situation on the basis of the same legal premises. First of all, there should be unanimity on the **basic legal qualification of stock lending** and the basic legal consequences resulting from it in terms of ownership and accompanying rights and obligations. Stock lending agreements entered into by the parties concerned could then build further on these legal premises. As a lot of issues would still be left to contractual freedom, there should be EU wide guiding principles or best practices recommendations.

The three ruling principles should be that
- there should be **no stock lending without the shareholder's explicit consent**
- the shareholder's rights, including and especially **the right to vote and the right to control this voting right, should at all times be safeguarded**
- there should be complete **transparency towards all concerned parties**, including the issuer.

As a consequence, the Recommendation should read as follows[4]:

"1. ***Member States should ensure that there is no ambiguity as to the civil law qualification of stock lending.***
~~*Stock lending agreements should contain provisions informing the relevant parties of the effect of the agreement with regard to the voting rights attaching to the transferred shares.*~~

[2] See art. 10, lett.b) of the Transparency Directive.
[3] Information would include a) the resulting situation in terms of voting rights; b) the chain of controlled undertakings through which voting rights are effectively held, if applicable; c) the date on which the threshold was reached or crossed and: d) the identity of the shareholder, even if that shareholder is not entitled to exercise voting rights under the conditions laid down in article 10, and of the natural person or legal entity entitled to exercise voting rights on behalf of that shareholder. See art. 12, par. 1 of the Transparency Directive.
[4] Deletions in strike through; additions in bold.

2. Member States should ensure that
***a)** shares can only be lent by financial intermediaries ~~where the investor~~ **provided the shareholder** has explicitly agreed to his shares being used for stock lending in the framework agreement with his financial intermediary **or otherwise**.*
b) financial intermediaries that are lenders monitor at all times what stock is the subject of stock lending agreements to allow them to comply with the provisions hereinafter.
3. Lenders should make best endeavours to discourage the practice of borrowing shares for the purpose of voting.
4. Stock lending agreements should safeguard the shareholder's exclusive right to control the voting rights attaching to the lent shares by both a) providing that the exercise of the voting rights by the borrower are strictly subject to the shareholder's explicit approval and b) including provisions to ensure the shareholder's direct or indirect exercise of such rights in practice.[5]
5. Member States should ensure that where the lender is not the shareholder, the latter will be duly and timely informed by the borrower of a) upcoming general meetings concerning lent shares and b) how he can exercise his voting rights directly or indirectly in practice.
6. Stock lending agreements should provide that borrowers have to return equivalent shares to those borrowed promptly upon the lender's request.
7. The lender should inform the issuer of stock lending agreements that result in a holding of stock representing 1 % or more of the voting rights, in a period running as of 15 days before the record date up to the date of the general meeting, disclose the identity of the shareholder and of the borrower.
8. Institutional investors should clearly disclose their policy with regard to stock lending.
9. The foregoing provisions should also apply to practices similar to stock lending insofar they imply a temporary transfer of voting rights."

III. CHAIN OF INTERMEDIARIES

1. DUTIES OF INTERMEDIARIES

Question 4:

Q 4.1: Do you consider that the duties of intermediaries in the voting process need addressing?
Q 4.2: If your answer is yes, would you consider recommendations along the following lines as adequate?

[5] The Commission might want to consider to state explicitly that non compliance with this provision has no effect on the validity of the exercised voting rights towards the issuer.

"1. Member States should ensure that before entering into relevant agreements, intermediaries explain to clients whether, and if so how, they will be able to give instructions about the exercise of voting rights.
2. Where a client is entitled to give instructions about the exercise of the voting right, Member States should ensure that financial intermediaries that are part of the chain of intermediaries between that client and the issuer either cast votes attached to shares in accordance with the clients' voting instructions or transfer the voting instructions to another intermediary higher up in the chain.
3. Financial intermediaries should keep a record of the instructions and provide confirmation that they have been carried out or passed on for a period of at least one year.
4. Member States should ensure that fees charged by intermediaries for the services referred to above do not exceed substantially the actual costs incurred by that intermediary.
5. Member States should ensure that intermediaries take the necessary measures to have the client's name registered in the register of companies which have issued registered shares. This obligation should not apply where the client objects to his name being registered.
6. "Client" within the meaning of this provision is the natural or legal person on whose behalf another natural or legal person holds shares in the course of a business."

As the Commission rightly pointed out, intermediaries are **key players** in the processes around general meetings. Issuers and shareholders rely on them not only to get **the notice to convene** the meeting swiftly through from the issuer to the shareholder, but also to make sure that information regarding the **identity of the shareholder** and, where applicable, his **voting instructions** reach the issuer in a timely manner. EALIC agrees that there is indeed an urgent need to address the duties that intermediaries should fulfil in these processes, because the deficient functioning of the chain of intermediaries presents one of the major obstacles to efficient cross-border voting.

However, EALIC believes that the recommendations proposed by the Commission as to the intermediary's role in the disclosure of the shareholder's identity and in the exercise of voting rights are **not satisfactory** (see hereinafter).

In the first place, the proposal does indeed **not acknowledge the need to identify the shareholder** although this is crucial to improving the dialogue between the shareholder and the issuer as well as to securing the integrity of the voting process (see hereinafter "2. Disclosure of investors"). The principle of disclosure of the shareholder's identity should be confirmed and promoted and any possibility to oppose the disclosure of the investor's identity, as suggested in paragraph 5 of the proposal, should be discarded. The Recommendation must not only provide for the intermediary's duty to identify the shareholder, but should also encourage Member States to remove all legal obstacles that intermediaries could be confronted to in complying with the said disclosure obligation, such as provisions in place in the area of privacy or data protection. It is also worthwhile to look at the example of Member States (for instance France and the UK) that provide for the positive obligation to identify the shareholder; non-compliance may result in the loss of dividend or of the voting right. In such case, intermediaries must not act against the effect of the sanction.

Secondly, the proposal does **not acknowledge the ultimate right of the shareholder or the ultimate investor to control the voting right** by casting a vote directly or giving a proxy. Improving the functioning of the chain of intermediaries must serve the objective of facilitating the exercise of voting rights by the ultimate investor. When the intermediary acts as a proxy holder, he must vote according to the voting instructions received or transfer the voting instructions to another intermediary higher up in the chain. In its current wording, the Commission proposed recommendation even seems to suggest that intermediaries ultimately control whether or not and how a shareholder can vote. It fails therefore to address the main issue at stake: to acknowledge the right of the shareholder to control the voting right[6] notwithstanding the fact that its shares are held through a chain of intermediaries. For instance, EALIC must strongly disagree with the proposed wording of paragraph 1 of the draft recommendation which, while in line with the need to make the investor aware about the exercise of voting rights, implies that the end investor will not necessarily be entitled to give voting instructions to the intermediary. On the contrary, it should be clearly spelled out that it is the shareholder, not the intermediary, who is entrusted with the rights attached to the shares and who, accordingly, can give instructions about the exercise of voting rights.

Last but not least, the various notions used in the proposed recommendation do not seem to be adequate. It is striking that the notion of shareholder does not appear in the text. The text seems to ignore the fact that a **client is not necessarily a shareholder**! It is however essential to make that distinction if we really want to improve the voting process to the benefit of the shareholder. Moreover the definition of client in the last paragraph should be corrected as its current wording implies a **limited definition of intermediary**. By using the notions "on whose behalf" and "holds shares", the definition suggests that the recommendation only concerns intermediaries who hold shares in the name and/or for the account of somebody else. However the proposed recommendation should not only envisage the intermediary as meant in Art. 13 of the Shareholder Rights Directive. It is obvious that all intermediaries who keep securities accounts or intervene otherwise in the processes around general meetings must be implied in the scope of the proposed recommendation. Moreover, one will find along the chain clients of intermediaries that are intermediaries themselves, in which case they are not shareholders. As a matter of fact, EALIC believes that it would be appropriate to define intermediaries in addition to client (as a matter of fact, the latter should simply be seen in its generic meaning).

The Recommendation should therefore be amended as follows:

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[6] This general principle is fully acknowledged by the Shareholders' Rights Directive: see Recital 3 "*Holders of shares carrying voting rights should be able to exercise those rights given that they are reflected in the price that has to be paid at the acquisition of the shares*" and Recital 11 "*Where financial intermediaries are involved, the effectiveness of voting upon instructions relies, to a great extent, on the efficiency of the chain of intermediaries, given that investors are frequently unable to exercise the voting rights attached to their shares without the cooperation of every intermediary in the chain, who may not have an economic stake in the shares. In order to enable the investor to exercise his voting rights in cross-border situations, it is therefore important that intermediaries facilitate the exercise of voting rights. Further consideration should be given to this issue by the Commission in the context of a Recommendation, with a view to ensuring that investors have access to effective voting services and that voting rights are exercised in accordance with the instructions given by those investors.*"

"1. Member States should ensure that ~~before entering into relevant agreements,~~ intermediaries, ~~explain to clients whether, and if so how, they will be able to give instructions about.~~ ***as a general principle, do whatever that is in their remit to contribute to a swift, timely and cost efficient communication of information regarding general meetings between the issuer and the shareholder, both downstream and upstream, including information regarding the notice to convene the general meeting, the identity of the shareholder and the number of shares held by him, the confirmation of the shareholder's attendance to the general meeting,*** *the exercise of voting rights,* ***proxy voting, voting instructions and all other information that is necessary to improve the efficient and sound functioning of general meetings.***

2. ***Moreover Member States should ensure that, as regards the duty to disclose the identity of the shareholder, intermediaries do whatever that is in their remit to contribute to a swift, timely and cost efficient identification, at any time upon request of the issuer.***

3. ***Member States should remove all legal obstacles that would stand in the way of communication of the information as meant in point 1 and point 2, in particular as concerns the disclosure to the issuer of the identity of the shareholder.***

4. Member States should ensure that before entering into relevant agreements, intermediaries explain the duties they have in the processes around general meetings to their clients. Member States should equally ensure that the relevant agreements between intermediaries and their clients include provisions to safeguard the shareholder's exclusive right to control and to exercise his voting right directly or indirectly.

5. ~~*2.*~~ *Where* ***a shareholder*** ~~*a client is entitled to*~~ ***gives voting*** *instructions* ~~*about the exercise of the voting right,*~~ *Member States should ensure that* ~~*financial*~~ *intermediaries that are part of the chain of intermediaries between* ***the shareholder*** ~~*that client*~~ *and the issuer****,*** *either* ~~*cast*~~ ***lodge*** *votes attached to shares in accordance with the* ~~*client*~~ ***shareholder****'s voting instructions or transfer the voting instructions to another intermediary higher up in the chain****, the latter having to comply with the same duty.***

6. ~~*3. Financial*~~ *Intermediaries* ***who receive voting instructions*** *should provide confirmation that they have been carried out or passed on and should keep a record of the instructions for a period of at least* ~~*one*~~ ***three*** *years.*[7]

7. ~~*4.*~~ *Member States should ensure that* ~~*fees charged by*~~ *intermediaries* ***comply with the recommendations of and use the standards***[8] ***developed by the industry to enhance cross-border voting. In any case, the cooperation of intermediaries in the areas indicated in this Recommendation should not give rise to any additional*** *fees.* ~~*for the services referred to above do not exceed substantially the actual costs incurred by that intermediary.*~~

8. ~~*5.*~~ *Member States should ensure that intermediaries take the necessary measures to have the* ***name of their client who is a shareholder,*** ~~*client's name*~~ *registered in the register of* ***the company*** ~~*companies*~~ *which* ~~*have*~~ *issued* ***the concerned*** *registered shares.* ~~*This obligation should not apply where the client objects to his name being registered.*~~

[7] The order of duties in this provision has been inversed.

[8] In the context of the works by Cesame, EALIC is a member of a Working group composed of representatives across industries to develop standards in this area that will be coherent with and complete where necessary the ISO standards 20022.

9. ~~*6.*~~ *"Client" within the meaning of this provision is the natural or legal person* ~~*on whose behalf another natural or legal person holds shares in the course of a business.*~~ ***who holds a securities account with an intermediary****.*
10. "Intermediary" within the meaning of this provision is any legal person who, in the course of a business, provides securities accounts to a shareholder or to another legal person who provides securities accounts."

2. DISCLOSURE OF INVESTORS

Question 5: Would you agree that the transparency directive, once implemented, will give a breakdown of voting rights and that further action at EU level would be premature?

Transparency Directive

EALIC couldn't possibly agree with the thesis that the Transparency Directive, once implemented, would provide for a breakdown of voting rights, nor that it would render other action at EU level premature. It should be reminded that the Transparency Directive, although a useful instrument, serves a **different purpose**. The Transparency Directive is part of the set of useful legislative instruments to improve the quality of information available to investors on companies' performance as well as on changes in major shareholdings. It is meant to contribute to better investor protection, enhanced investor confidence and a better functioning of European capital markets. It is not meant to bring the shareholder and the issuer closer to each other. Moreover, the notification requirements of the Transparency Directive i) only apply for **very large shareholdings**: 5 % and more of the capital, ii) only apply in case certain (important) shareholding **thresholds are exceeded or not any longer exceeded** and iii) apply at that **very moment in time only**. The Transparency Directive lays notification obligations with the shareholder (and by extension to some other parties in their capacity of holding shares). However it is **not prescribing any disclosure duties for the intermediaries** appearing in the long chain of intermediaries separating the shareholder from the issuer. Finally as to the **sanctions** applicable in case of violation of the notification requirements the Transparency Directive refers the matter to the Member States. It remains to be seen whether any sanctions will be capable of making the system waterproof.

The Transparency Directive in itself will not allow for the kind of transparency of shareholders the issuers are so much longing for. Issuers are experiencing many barriers in their search for transparency as we will explain hereinafter.

Chain of intermediaries

Today's shareholding system is characterised by a very high level of foreign shareholdings, thanks to the ongoing integration of the European markets. The Commission is fully aware of the fact that in cross-border shareholdings, there is a **chain of intermediaries** separating **the issuing company from the shareholder**. Sometimes, those intermediaries are recognised as the shareholder. Sometimes they act like or, at least, give the appearance of a shareholder. Due to the number of intermediaries, identification of the (real) shareholder is very burdensome if not impossible for issuers and questions arise as to who is ultimately entitled to control the voting right. Issuers are **not able to look through the chain** and know their (real) shareholders. They are surrounded by a thick mist.

Of course, companies do attempt to identify their shareholders, but they hardly ever reach the end of the chain. Too often they are stopped at the level of the custodians and other financial intermediaries. Omnibus accounts don't exactly help to bring more clarity. In addition, there is a lack of compatible electronic systems that allow for easy and quick communication across the EU. Language barriers should also not be underestimated. Where disclosure obligations exist, their implementation often turns out to be costly, slow and inefficient and largely **dependent on the willingness of intermediaries** to connect the two sides.

Dialogue with the shareholder

This lack of transparency threatens to jeopardize the meaningfulness and the good order of general meetings - the forum per excellence for the shareholder to express his opinion and have real impact! Companies don't know their shareholders and can therefore not motivate them to attend the general meetings. For the same reason, they cannot verify whether the real shareholder's voting entitlement is safeguarded. The position of that shareholder in the cross-border voting process is highly uncertain. How can companies be sure that the resolutions will be voted by those who have a true interest in the company?

In the context of general meetings, identification of the shareholder and unambiguous determination of who ultimately controls the right to vote is critical for a number of reasons:
-to enhance shareholders participation and involvement in the general meetings
-to prevent abuse of voting rights and over-voting. It is in the interest of both shareholders and issuing companies that only those with an undisputed entitlement to vote actually take part in the ballot.
-the current confusion may lead to the voting rights not being exercised at all.
-transparency must enable the exercise of statutory rights reserved to shareholders.

Identification of the shareholder would allow issuers to have a **sound and permanent corporate dialogue** with the actual shareholder: the person who takes a genuine, economic interest in the affairs of the company. Issuers could then encourage shareholders to participate and cast their vote in the best possible knowledge of the company's specific affairs, and thus avoid that a general meeting becomes a box ticking exercise or, worse even, that a small percentage of shareholders decide about the future

for 100 % of the shareholders. The more shareholders vote, the less the risk of distortion by activist shareholders. Increasing attendance numbers can also be important in order to reach the **quorum** provided for by law. Even in those countries, where the threshold for shareholders' participation in the general meeting are relatively low, it is still difficult for companies with widespread share ownership to reach the quorum, as large stakes are held by non residents who do not easily participate to the general meeting. Finally identification should benefit the **transparency of the voting process**, ensure its **integrity** and enable the exercise of statutory rights reserved to shareholders.

Beyond the context of the general meeting, a permanent dialogue is needed in order to explain the company's goals and the strategy on the medium and long term. Such will pave the way for long term relationships and for **convergence of interests**, which is the ultimate goal from the issuers' perspective.

Legal and practical measures to be recommended

We have a strong belief that **both legal and practical measures** are required to overcome the hurdles described above. The legal uncertainty cannot be removed by market forces alone, nor can we leave it to contractual provisions taken between the ultimate shareholder and his intermediar(y)(ies). Both a legal framework and the industry's co-operation are necessary to enable issuers to establish an **identification trail that leads as close as possible to the last person in the chain,** the person that holds the economic interest in the shares. In this respect we wish to point out that the quest for shareholder identification does not stand in the way of trusts or fiduciary companies. That is a completely different situation as explicitly envisaged in question 4.2.2. of the Commission's fact-finding questionnaire (page 3) of 30 April 2007 concerning the possible recourse to fiduciary intermediaries.

EALIC welcomes the Shareholder Rights Directive. It represents a good step forward in terms of facilitating cross-border voting. We are happy that it establishes the concept of shareholder qualification, including identification, on a given date before the general meeting, the so-called "record date". The record date is key in determining admission to and participation in the general meeting, the exercise of the voting right, including by proxy and upon instructions. It thus provides issuers with a positive right to have the shareholder identified and lays the entitlement to control the voting right with the person that qualifies as a shareholder.

However, our feeling is that the Directive is **not very ambitious** in the area of identification and disclosure requirements. It mentions the issue only in a "matter of fact" manner in the context of a few provisions. Moreover, as to the person on behalf of whom the "recognised shareholder" is acting, say the "real" or "ultimate" shareholder, the Shareholder Rights Directive merely acknowledges implicitly the possible existence of disclosure requirements in the "applicable law" (which is the law of the issuing company's registered office). What is more, the Directive actually puts limits on these disclosure requirements rather than providing disclosure obligations concerning the "real" or "ultimate" shareholder at community level. Last but certainly not least, the Directive remains silent as to the role the intermediaries, although key actors in the identification process, should play.

Therefore the Recommendation must now pave the way for a **real set of principles** and make sure that they will be actually be **complied with in practice by the intermediaries**. Issuers must have the possibility to trace back their shareholders along a trail that leads as close as possible to the actual shareholder, the one who bears the economic risk.

It is of key importance that intermediaries disclose the **identity of the shareholder and the number of shares held by him**. We stress that they should have such duty not only in the course of the processes around general meetings, but also **at any time upon request of the issuer**. As said here above, financial operations that can influence voting entitlement, such as stock lending, must be subject to common principles of best practice as we propose in the amended recommendation above.

The proposed recommendation is addressing itself only to **intermediaries**. It would be useful to **address the shareholders also directly**. As we said above, some Member States provide that non disclosure of the identity of the shareholder may result in the loss of dividend or of the voting right.

Not an isolated request

Finally EALIC would like to point out that European issuers **do not stand alone** in their request for shareholder transparency. Investors, proxy voting agencies and corporate governance networks to name but a few share the issuers' concern. We wish to refer to the Dutch example for instance. In its excellent Report released in May 2007, the Dutch Corporate Governance Code Monitoring Committee recommends that legislation be developed in order to enable the company to establish the identity of a shareholder (the person beneficially entitled to the shares). The report literally states that :"*The Monitoring Committee considers that, in view of the increased corporate transparency, the shareholders too cannot escape the requirement of greater openness, certainly if they wish to play an active role in the company.*"[9] In some countries, the lack of transparency has given rise to malpractice and abuse of voting rights. The U.S. Securities and Exchange Commission (SEC) has recently addressed the issue on the occasion of a Roundtable on Proxy Voting Mechanics where the question was raised whether beneficial owners should continue to have the ability to object to having their names disclosed. In 2006, a NYSE Working Group noted that efforts to improve the ability of issuers to communicate with their beneficial owners should be supported.

EALIC would also like to point out that the lack of transparency is not only an issue in case of bearer shares: even companies that have only registered shareholders complain that they are not able to know their shareholders anymore! Again this is due to the fact that shares are all too often being registered under the name of intermediaries. Therefore the suggestion that is sometimes made that companies should opt for nominative shares only in order to know their shareholders does not offer any solution.

[9] Corporate Governance Code Monitoring Committee report, pages 8 and 21. See the full Report on http://www.commissiecorporategovernance.nl/page/downloads/Monitoring_Committee_Advisory_Report_May_2007.pdf.

The Commission can not remain blind for the growing request for more shareholder transparency and must realise that the time has come to take very concrete measures to the benefit of all stakeholders.

IV. MANAGEMENT COMPANIES OF INVESTMENT SCHEMES

Question 6: Do you think there is a need for a recommendation along the following lines?

"1. Management companies, the regular business of which is the management of collective investment schemes, shall be deemed to be 'clients' for the purposes of the draft recommendations set out in section V.1.

EALIC concurs with the proposed recommendation provided its amendments to the recommendations set out in section V.1., addressed here above under III.1. are accepted. As said above, these amendments make it clear that there is a difference between a client and a shareholder. They are meant to make sure that not any client whatsoever be treated as a shareholder. There is no reason to treat management companies differently. Out of respect for the actual shareholder's voting entitlement, we must not confuse the different capacities a management company can have.

V. OTHER SUGGESTIONS

In our view, the following issues should also be taken into account while taking measures to facilitate cross-border voting:

1. The Hague Convention

EALIC would like to draw the Commission's attention to the possible impact the adoption of the **Hague Securities Convention** in the EU could have on the exercise of shareholders' rights in the European Union, as it could render the EU law in the area of shareholders rights inapplicable.

In case of **conflict of law,** the Hague Convention determines **the law applicable to the legal nature and effects of a credit of securities to an account held through an intermediary.** The entitlement to exercise the voting rights is directly affected where the applicable law as determined by the Convention lays such entitlement with the account holder.

To determine the applicable law, the Hague Convention would replace **the 'location of account' or "lex rei sitae" principle** (on which the EU provisions are based) by a **free choice of the applicable law, subject to a reality test,** to be defined in the contract

between the intermediary and the securities account holder. In practice the reality test that requires the relevant intermediary to have an office engaged in the activity of maintaining securities accounts in the State which law is chosen, would be too easily complied with, *De facto* there would be no restriction on the free choice of the applicable law by the two contracting parties of the securities account and the Hague Convention would therefore allow European accounts to be ruled by non-European laws as the most **dominant party would obviously impose his choice of law**.

The proposed rules contain the not unrealistic risk that **a small number of global players would impose their preferred law worldwide.** By doing so they would be able to pool their securities accounts worldwide under the same law, and to realise economies of scale by applying to them the same legal provisions and, as a consequence, technical systems and processes, all this to the detriment and expense of parties established in the EU.

If that would be the case, the exercise of voting rights in European general meetings could be seriously disrupted. Therefore, EALIC encourages the Commission to **withdraw its proposal of 15 December 2003** to the Member States to sign the Hague Securities Convention. EALIC concurs with the recommendation of the European Parliament (14 December 2006), that the Commission conduct a thorough impact assessment before proposing any change of the current 'acquis communautaire' regarding the applicable law to the rights of the account holders in the EU.

2. The Unidroit Convention

In addition to The Hague Convention, the UNIDROIT draft convention on substantive rules regarding intermediated securities is also **threatening the exercise of voting rights by the actual shareholder**.

Issuers are concerned that the scope and purpose of the Convention have become substantially broader than initially envisaged. We understand and appreciate that the Convention has its merits where it aims to harmonize the situation of securities credited to a securities account. The rights and obligations derived thereof against the intermediary who provides the account, on the one hand and those against third parties who have an interest in the intermediary, on the other hand, are to be approximated. The rights of the account holder must be protected in case of insolvency or similar procedure regarding the patrimony of the intermediary and it must be made clear that the securities accounts belonging to account holders do not form part of the property of the intermediary available for its creditors. However the convention must stick to this clear and well defined purpose and **refrain from interfering with corporate law** regarding securities and the relationship between shareholders and issuers, including the rights granted to shareholders by and to be exercised against issuers as laid down by the Directive and completed by the currently proposed Recommendation. In its current wording, Unidroit would pave the way for arbitrary proxy voting by intermediaries. It is therefore of the utmost importance that the Convention respects the integrity and sovereignty of such EU legal framework. EALIC encourages the Commission to monitor the developments carefully and act where necessary to **preserve the "acquis communautaire".**

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