

Shareholder Rights Directive II (SRD II)

REGULATORY SUMMARY

INTRODUCTION

The Shareholder Rights Directive II (SRD II) is a European Union (EU) directive, which sets out to strengthen the position of shareholders and to reduce short termism and excessive risk taking by companies. It amends SRD I which came into effect in 2007, with the objective of improving corporate governance in companies whose securities are traded on EU regulated markets.

SRD II is an amending directive that will require transposition into each Member State's national law.

Implementation of the Directive is due to take place in two phases: 10th June 2019 for the initial transposition into Member State national laws, and 3rd September 2020 for core operational changes applicable to Articles 3A, 3B and 3C.

OVERVIEW

- SRD II establishes requirements in relation to the exercise of certain shareholder rights attached to voting shares of companies. This applies to companies (referred to also as issuers) that have their registered office in the EU and their shares listed on an EU regulated market.

It also establishes specific requirements to encourage shareholder engagement, in particular for the long-term. The requirements apply in relation to:

- The identification of shareholders;
- The transmission of information to shareholders;
- The facilitation of exercise of shareholders rights;
- Transparency of institutional investors;
- Asset managers and proxy advisors; and
- Remuneration of directors and related party transactions.

AIMS OF SRD II

It was felt that the financial crisis revealed:

- Shareholder supported managers' excessive short-term risk taking;
- Monitoring of investee companies and engagement by institutional investors and asset managers was often inadequate; and
- Complex chains of intermediaries render the exercise of shareholder rights more difficult and this can act as an obstacle to shareholder engagement.

SRD II therefore aims to:

- Improve corporate governance via encouraging long-term shareholder engagement;
- Discourage excessive short-term risk taking;

- Improve the ease with which a company can identify its own shareholders as a means of facilitating shareholder engagement;
- Improve transparency between Institutional investors and asset managers with regards to shareholder engagement;
- Grant shareholders the right to hold a binding or advisory vote on remuneration policy; and
- Formalize market practice through the changes to Article 3 around the identification of shareholders, the transmission of information and facilitation of exercise of shareholder rights.

Scope and who does it apply to?

The Directive establishes requirements in relation to certain shareholder rights attached to voting shares of companies that have their registered office in the EU and their shares listed on a regulated market in the EU.

The Directive also applies to:

- Intermediaries used by shareholders
- Institutional investors and asset managers to the extent that they invest in in-scope shares
- Third country intermediaries when they provide services to in-scope shares

Main changes from SRD I to SRD II

- The main change from SRD I to SRD II is the significant change that has been made to Article 3 which now gives companies the right to identify their shareholders. This creates an obligation on intermediaries to transmit the necessary information to determine shareholder identity.
- Intermediaries also have to transmit relevant information from the company to the shareholder to facilitate the exercise of their shareholder rights. Intermediaries must publicly disclose what they charge for these services and costs must be non-discriminatory and proportionate.
- For institutional investors and asset managers, there are additional requirements to publish an engagement policy and disclose annually how the main elements of their investment strategy contribute to the medium to long-term performance of their assets.
- Proxy advisors must adhere to a code of conduct and disclose information to show how their voting recommendations are accurate and reliable.
- Shareholders have the right to vote on remuneration.

Continued

Intermediaries: Intermediaries will be required to facilitate a company's right to identify its shareholders and to facilitate the exercise of shareholder rights.

It is not just intermediaries located in the EU that fall in scope; the Directive applies to any non-EEA firm who holds in scope shares.

Requirements on Institutional Investors: SRD II requires Member States to ensure that institutional investors disclose to the public how their equity investment strategy is aligned with the profile, the duration of their liabilities, and how it contributes to the medium to long-term performance of their assets.

Remuneration: SRD II mandates that shareholders be given the right to vote on the company's remuneration policy for directors and that directors are paid in accordance with the remuneration policy approved by the general meeting. The aim of this requirement is create a better link between pay and performance of company directors.

How does this Impact BNY Mellon Products and Services?

Every entity in the custody chain will need to know their status and specifically, in what capacity they are acting: an intermediary, a final intermediary or shareholder.

At a high level, intermediaries will be required to:

- Receive and pass on requests for shareholder identification to intermediary clients;
- Respond to such a request directly to the issuer or the issuer's appointed third party the day after record date or the date of receipt of the request, whichever comes later;
- Receive and pass on general meeting notifications;
- Facilitate an end investor's voting for the general meeting;
- Where acting as the "final" intermediary, provide confirmation of entitlement to participate to the shareholder as well as ensuring that the number of units voted on is consistent with the shareholders entitled position;
- Differentiate at a securities account level end shareholder or intermediary status; and
- Transmit notifications relating to general meetings and corporate events the same day it was received (unless if received after 16:00, in which case by 10:00 the following business day) providing we have received them in electronic and machine readable formats.

Shareholders:

- Have the right to receive general meeting notifications and exercise their right to vote. Intermediaries are required to provide a service to facilitate this.

BNY Mellon is currently assessing the full impact of these requirements on our current products and services.

Changes will be required to the way in which we provide information on general meeting notification as today this is an opt-in service and shareholders can choose not to receive these messages. The Directive now requires intermediaries to inform shareholders and downstream intermediary clients of these events. Any client of BNY Mellon acting as intermediaries themselves, will also be obliged to notify their intermediary clients or shareholders downstream.

There is also a new disclosure process which sets out a new messaging structure and data fields that must be provided, for example LEIs and third party information. BNY Mellon is reviewing the data we have available and may in due course require some additional information from clients.

For further information please contact your BNY Mellon Relationship Manager.

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