



**CORPORATE GOVERNANCE**  
**MANUAL**  
**2013 EDITION**

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## INTRODUCTION

In recent years institutional investors have felt an increasing responsibility to make use of the rights attaching to the shares they hold. This sense of responsibility has grown as a consequence of the legal reinforcement of the position of the general meeting of shareholders (hereafter: “general meeting”), due to the conferral of a number of new rights in 2004 and the enshrinement in law of the Dutch corporate governance code in that same year. The widening of shareholders’ powers was largely prompted by the endeavours of the legislator and the Dutch Corporate Governance Committee to restore investor confidence in the management and supervision of listed companies, this confidence having been impaired by a number of notorious accounting scandals and bankruptcies shortly after the turn of the century. According to the legislator and the Corporate Governance Committee, the strengthening of the position of the general meeting was a necessary pre-condition for the improvement of the checks and balances at the listed companies, in order to reduce the risk of new scandals. The Netherlands was not the only country, incidentally, where the position of shareholders has been reinforced in recent years; this happened in large number of other countries as well.

On the basis of the idea that institutional investors who operate globally hold most of the shares in listed companies and manage other people’s money, a more active and engaged role is expected of this category of investors in particular. In the words of the Corporate Governance Committee, institutional investors should act primarily in the interest of their ultimate beneficiaries and they have a “responsibility to the ultimate beneficiaries or investors and the companies in which they invest, to decide, in a careful and transparent way, whether they wish to exercise their rights as shareholder of listed companies.”

A special paragraph on institutional investors was included in the Dutch Corporate Governance Code in order to codify the existing best practices for institutional investors with regard to corporate governance. According to the code, institutional investors should have a policy on exercising voting rights in companies in which they invest. In addition, they should report on the implementation of that policy and on the concrete voting behaviour at the general meetings. The legislator has underlined these obligations by enshrining what is known as the “apply or explain” principle for institutional investors in the Financial Supervision Act (Netherlands). With effect from the financial year 2007, every institutional investor established in the Netherlands is required by law to give an account of its compliance with the principles and best practice provisions in the Netherlands corporate governance code that apply to it.

The introduction of this statutory duty is also connected with society’s increasing interest in the question of how shareholders – and institutional investors as well, by extension – exercise the rights assigned to them. What responsibilities do shareholders have?

Eumedion regards it as one of its tasks to provide the institutional investors among its members with support in developing and implementing a voting policy and in accounting for the implementation of the voting policy. Eumedion has already contributed to this in the last few years, by making recommendations to the institutional investors which are its members. These recommendations are contained in the publications “Recommendations on the delegation of power to issue shares” (January 2008), “Recommendations on the authorization to repurchase own shares and on accountability for the dividend policy” (July 2008), “Principles for a sound remuneration policy for members of the management board of Dutch listed companies” (October 2009; amended in 2011 and 2012), “Best Practices for Engaged Share-Ownership” (June 2011) and “Guidance for the explanatory notes to the nomination for (re)appointment of the statutory auditor” (October 2011) which are published in this Corporate Governance Manual 2013, so that all the relevant information on the development and implementation of a voting policy can be found in one place.

#### *Reading guide*

This manual provides the institutional investors which are members of Eumedion with guidelines for taking part in and voting at the general meetings of the Dutch listed companies. This version of the manual is an update of the 2010 Manual. The first edition was published in 2004, by the predecessor of Eumedion, the Corporate Governance Research Foundation for Pension Funds (SCGOP).

The manual consists of three sections. The first section contains a summary of the *rights* of shareholders in Dutch listed companies; this section provides a number of reference points or recommendations for each (standard) item on the agenda for a general meeting, which can be consulted when deciding on voting behaviour and with regard to asking questions during the general meeting. The second section contains an overview of shareholders’ *responsibilities*, particularly those of institutional investors who invest in Dutch listed companies. The third section comprises a number of practical aspects of casting a vote at the general meetings of Dutch listed companies.

Eumedion hopes that this new version of the Corporate Governance Manual will contribute towards further professionalization and greater depth of the voting policy of institutional investors. The text of the 2013 manual was closed on 18 December 2012 and will be updated regularly on the basis of new legislation and regulations, best practices and other developments.

The text of this manual was formulated with the greatest possible care. We are, however, unable to guarantee that the information contained in this manual is still accurate on the date on which it is received, or will continue to be so in future. Eumedion cannot, therefore, be held responsible for decisions taken on the grounds of the information in this manual.

## **SECTION I: SHAREHOLDERS' RIGHTS IN THE NETHERLANDS**

## **I.1 Summary of shareholders' rights**

According to the Dutch corporate governance code, the general meeting must be able to exert such influence on the policy of the management board and supervisory board of the company that it plays a fully-fledged role in the system of checks and balances at the company (principle IV.1 of the Dutch corporate governance code).

Partly on the basis of this point of view, the legislator has granted the following legal rights to the general meeting as an organ of Dutch listed companies:

### *Appointment and dismissal of members of the management board and of the supervisory board*

- a) appointment, suspension and dismissal of members of the management board, in which context it should be noted that management board members of a statutory two-tier company are appointed by the supervisory board (section 2:134 Civil Code (Netherlands), hereafter the "Civil Code"; see section 2:162 and 2:164a Civil Code for statutory two-tier companies);
- b) appointment, suspension and dismissal of members of the supervisory board, in which context it should be noted that the general meeting of statutory two-tier companies only has the option of collective dismissal of the members of the supervisory board (section 2:142, 158 par. 4, 144, 161a, 162a Civil Code).

### *Accountability of (financial) policy and supervision*

- c) request of relevant information (section 2:107a Civil Code);
- d) granting of discharge to members of the management board and members of the supervisory board (section 2:101 par. 3 Civil Code);
- e) adoption of the annual report (section 2:101 par. 3 Civil Code);
- f) appropriation of the profit and declaration of the dividend (section 2:105 in conjunction with 101 par. 6 Civil Code; best practice provision IV.1.5 of the Dutch corporate governance code)<sup>1</sup>;
- g) appointment of the statutory auditor, unless stipulated otherwise (section 2:393 par. 2 Civil Code).

### *Remuneration*

- h) adoption of the remuneration policy for the management board (section 2:135 par. 1 Civil Code);
- i) adoption of the remuneration for the supervisory board (section 2:145 Civil Code);
- j) approval of share schemes and option schemes (section 2:135 par. 3 Civil Code).

### *Internal structure*

- k) amendment of the articles of association (section 2:121 Civil Code);

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<sup>1</sup> A distribution charged to the reserves also requires a resolution of the general meeting of shareholders.

- l) resolution on a proposal by the management board to continue or discontinue the two-tier board system after the company no longer meets the legal criteria for application of the two-tier system (section 2:154 par. 4 Civil Code);
- m) conversion (section 2:18 in conjunction with 71 Civil Code);
- n) legal merger (section 2:317 in conjunction with 330 and 331 Civil Code);
- o) split-off (section 2:334 Civil Code);
- p) designation of a representative in the event of conflicting interests (section 2:129 par. 6 and 2:140 par. 5 Civil Code);
- q) issue of shares or delegation of this power to another organ (section 2:96 Civil Code);
- r) exclusion of the pre-emption right in the event of the issue of shares, or delegation of this power to another organ (section 2:96 Civil Code);
- s) purchase of own shares, or delegation of this power to another organ (section 2:96 Civil Code);
- t) reduction of capital (withdrawal of shares) (sections 2:99 and 2:100 Civil Code);
- u) instructions to file for bankruptcy (2:136 Civil Code);

*Public offer and other decisions on a major change in the identity or character of the company*

- v) approval of management board decisions concerning a significant change in the identity or character of the enterprise or company (section 2:107a Civil Code);
- w) discussion of a public bid for the shares of the company (section 18 par. 1 Decree on Takeover Bids Financial Supervision Act [Netherlands]);
- x) the exemption of a shareholder or group of shareholders acting in concert from the obligation to make a public bid for the shares<sup>2</sup> (section 2 Exemptions Decree Financial Supervision Act [Netherlands]).

*Logistics*

- y) designation of the official language of the annual report and the annual accounts (section 2:391 par. 1 and 2:362 par. 7 Civil Code);
- z) distribution of information to shareholders by way of electronic means of communication (section 5:25k Financial Supervision Act [Netherlands]).

In addition to the above legal rights, the Dutch corporate governance code contains a number of rights for the general meeting. The Dutch listed companies have no obligation to grant these rights to the general meeting, but in the event of their failure to grant these rights, they must provide an explanation for this decision. The following rights are involved:

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<sup>2</sup> A resolution of this nature must be passed with 90% of the votes cast. The votes of the shareholder or group of shareholders acting in concert that is the subject of the proposed exemption are not counted as votes cast. It is also stipulated that the passing of resolutions in the general meeting should take place at a time that is no more than three months in advance of the acquisition of overall control by the shareholder or group of shareholders in question.

- a) discussion of the policy on reserves and dividends, in particular the amount and purpose of the reserve and the amount and type of the dividend (best practice provision IV.1.4 of the Dutch corporate governance code);
- b) discussion of each substantial change in the corporate governance structure of the company and of compliance with the Dutch corporate governance code (best practice provision I.2 of the Dutch corporate governance code).

Resolutions are passed by a simple majority of the votes cast at the meeting, unless a qualified majority and/or a quorum is stipulated by law or in the articles of association. A legal departure applies, for example, in the event of the cancellation of a nomination for the appointment of a member of the supervisory board, or in the case of the dismissal of the supervisory board of a statutory two-tier company (quorum) and when excluding or limiting the pre-emption right in the event of the issue of new shares (qualified majority of votes if less than half of the issued capital is present at the meeting). The articles of association of Dutch listed companies often include the stipulation that greater, super or qualified majorities are required for resolutions concerning an amendment to the articles of association, the dissolution of the company, and the dismissal of members of the management board and/or supervisory board (on the initiative of one or more than one shareholder). It is common to require a two-thirds majority of the number of votes cast representing at least half of the issued capital.

Besides the above-mentioned powers of the general meeting as an organ of a Dutch listed company, individual shareholders or groups of shareholders also have certain rights:

- a) shareholders who singly or jointly represent at least 1% of the issued capital or who hold shares with a collective market value of at least € 50 million are entitled to put forward subjects to be dealt with at the general meeting<sup>3</sup>. The articles of association may contain lower thresholds (section 2:114a Civil Code);
- b) shareholders who individually or jointly represent at least 10% of the issued capital can, on their request, be authorized by a court to convene a general meeting. The articles of association may contain a lower threshold (section 2:110 Civil Code);
- c) a shareholder who represents 95% of the issued capital is entitled to buy out the remaining shareholders (section 2:92 Civil Code and 2:359c Civil Code);
- d) the right to offer the shares to the party which represents at least 95% of the issued capital as a result of a public bid (section 2:359d Civil Code);

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<sup>3</sup> The Act on amending the Financial Supervision Act, the Securities (Bank Giro Transactions) Act and the Civil Code in response to the advice of 30 May 2007 from the Corporate Governance Code Monitoring Committee sets the statutory threshold at 3% of the issued capital and abolishes the nominal value. However, the decision to increase the threshold in the articles of association is a decision that should be adopted by the general meeting of shareholders. The Act will enter into force on 1 July 2013.

- e) the right to submit a request for indemnification if the shareholder has voted against a merger resolution, when the acquiring company is a company incorporated under the law of another member state of the European Union or the European Economic Area (section 2:333h Civil Code).
- f) shareholders who individually or jointly represent a certain interest in a company can ask the Enterprise Section of the Amsterdam Court of Appeal to institute an inquiry into the running of a company. Shareholders of companies with an issued capital of more than € 22.5 million require a shareholding of at least 1% of the issued capital or a collective market value of at least € 20 million. Shareholders of companies with an issued capital of less than € 22.5 million require a shareholding of at least 10% of the issued capital or a collective nominal value of at least € 225,000. The articles of association may contain lower thresholds (section 2:346 Civil Code);
- g) every shareholder can demand of the Enterprise Section that the annual report be corrected (section 2:447 in conjunction with 2:448 Civil Code);
- h) after publication of the notice for a general meeting of shareholders, a shareholder with an economic interest, either alone or together with others, of at least 1% of the issued capital or who holds shares with a market value of at least € 250,000 is, in the near future, enabled to distribute information to other investors who are identified by the issuer. The information must be related to an item on the agenda of the general meeting. The issuer is required to pass the information on to the other identified investors with the utmost speed, in any event within three working days. This 'passing on obligation' can be fulfilled by sending emails to investors or by publishing the shareholder's information on the issuer's website. The issuer may refuse to pass the information on if the information:
  - a. is submitted too late (later than seven days before the date of the general meeting);
  - b. gives an incorrect or misleading impression;
  - c. is of such a nature that it would not be reasonable or fair to expect the issuer to pass it on.<sup>4</sup>

Shareholders can, furthermore, also initiate (other) proceedings in civil law or administrative law (by using the Class Action [Financial Settlement Act], by taking part in class actions against Dutch listed companies whose shares are [also] listed or traded on a stock exchange in the United States, or by lodging an appeal with the Appeals Board for Trade and Industry against a decision by the Netherlands Authority for the Financial Markets [hereafter the "AFM"]).

## **1.2 Tools for Eumedion members in assessing the items on the agenda for a general meeting**

In the following paragraphs Eumedion provides a number of tools for assessing subjects that frequently appear on the agendas of general meetings of Dutch listed companies. The tools are not exhaustive and are intended to be taken into consideration when reaching a decision on how to vote or on the discussion at the general meeting. Eumedion has prepared recommendations on a number of specific

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<sup>4</sup> This right is part of the Act mentioned in footnote 3.

items on the agenda. The recommendations given in some paragraphs must never lead blindly to the issue of specific voting proxies. Institutional investors will always have to form an opinion on their voting behaviour – on the basis of expert external advice on each item on the agenda at each company, if required – a process in which the circumstances of the case will weigh heavily.

### **I.2.1 Discussion of the annual report**

This part of the agenda is not a voting item; the report of the management board and the report of the supervisory board on the past financial year are discussed under this item on the agenda.

The following are points for attention in relation to the discussion of the annual report:

- Is sufficient and readily comprehensible information included about the mission, the strategy and the operational targets?
- Is a readily comprehensible risk paragraph included and a clear description of the internal risk management and control systems?
- Does the annual report contain a description of the principal risks related to the company's strategy, also including the environmental and social risks?
- Does the annual report contain a description of the company's risk profile: the attitude towards the principal risks for the company (risk tolerance) and, if shown, the company's vulnerability to manifestation of the risks?
- Does the annual report contain a description of the issues that the management and/or supervisory board considered in relation to the financial statements (including the main items of the auditor's letter to the management and supervisory board) and how these issues were addressed?
- Does the annual report contain a description of the company's statutory auditor rotation or tendering policy and disclosure regarding the current tenure of the incumbent audit firm?
- Does the annual report contain a description of the company's approach to the use of the statutory auditor for non audit related services? If this approach allows for non audit related services by the statutory auditor what steps have been taken to protect statutory auditor independence.
- Does the annual report contain a specific continuity analysis, including:
  - a clear overview of the group structure, i.e. the legal ownership structure (including subsidiaries and the percentage of shares that is owned by the parent company);
  - the financial structure;
  - dividend and share buy back policy;
  - the solvency and liquidity ratios;
  - transparency on financial ratios to which companies should comply according to their bank covenants and the 'results';
  - the governance structure, a.o. the shareholder structure in case of a controlling shareholders;
  - the integration of meaningful acquisitions and effectuating disinvestments;

- scenario analyses in which a.o. social and environmental opportunities and threats that are material for the company's sector are analysed?
- Is the explanation of the supervisory and advisory tasks of the supervisory board included in the report of the supervisory board, and is this sufficiently extensive and transparent? Is the report on the compliance with the Dutch Corporate Governance Code acceptable to institutional investors? Are the reasons stated for any non-compliances acceptable to institutional investors and not clichés?
- Is the remuneration report sufficiently clear and transparent? Does it contain sufficient information on the standards on the basis of which short-term bonuses are paid and long-term bonuses granted? Is all the information required on the grounds of the Dutch corporate governance code included in the remuneration report? Has the company taken into account the Eumedion principles for a sound remuneration policy for the members of the management board of Dutch listed companies (Appendix I)?
- Has the company included a clear corporate social responsibility paragraph in the annual report or has the company a separate sustainability report?
- Does the annual report contain an overview of the key performance indicators related to environmental and social performance of the company which are important for the investment process and for the analysis of the company by analysts and shareholders?
- Has an independent external party, e.g. the statutory auditor, provided assurance on the reported sustainability information?
- Is a clear and transparent summary included of the (potentially usable) anti-takeover measures and has the management board explained why the existing anti-takeover measures should be retained?
- Has the company implemented the points for attention referred to in paragraph III.1 with regard to the organization of the general meeting?

### **I.2.2 Adoption of the financial statements**

Under Dutch law, this is a voting item at the general meeting. The consequence of non-adoption is that no dividend can be paid and no own shares bought (subject to the condition that the general meeting has agreed to this; see paragraph I.2.14). The general meeting is unable to alter the financial statements during the meeting, but can make proposals for alterations. The statutory auditor must be consulted first for this purpose and must issue an opinion accordingly. A new meeting has to be convened to adopt the annual accounts.

The following are points of reference for the proposal to adopt the financial statements:

- Has the statutory auditor issued an unqualified opinion, a qualified opinion or a disclaimer of opinion?

- Has the management of the company offered sufficient insight into the accounts and the standards used to give assessments and estimates of asset items and liability items?
- Has the company changed over to different accounting principles without adequate explanation?
- If there are current claims against the company and claims that can reasonably be expected, has a reserve been created for this purpose?
- Are the accounting principles still up-to-date (going concern, changed market conditions)?
- Have any recommendations made by the AFM or the Enterprise Section of the Appeals Court in Amsterdam with regard to the accounts of the company in question been implemented?

### **I.2.3 Corporate governance policy**

This is (at least) a point for discussion during the general meeting. Companies can choose to put their corporate governance policy to a vote at the general meeting.

The following are points for attention in relation to this item on the agenda:

- Is the corporate governance policy being put to a vote at the general meeting, as recommended by Eumedion?
- Does the company apply the provisions of the Dutch corporate governance code to a substantial extent?
- Is the report on the compliance with the Dutch corporate governance code adequate? Are the reasons given for any instances of non-compliance acceptable to institutional investors and not clichés?
- It would be logical to ask critical questions and express doubts about proposals for or reports of an increase in the number of provisions that are not complied with.

### **I.2.4 Dividend policy and profit distribution**

This is (at least) a point for discussion at the general meeting. Companies can choose to put their dividend policy to a vote at the general meeting.

The following are points for attention in relation to this item on the agenda:

- Has the company taken into account the Eumedion recommendations on accountability of the dividend policy (see Appendix III)?

### **I.2.5 Appropriation of the profit and the amount of the dividend**

This is a voting item at the general meeting. The general meeting can, however, change the proposal during the meeting. The financial statements must first be altered for this purpose, which means that the statutory auditor must be consulted and must issue an opinion. A new meeting has to be convened to adopt the amount of the dividend.

The following are points of reference in this context:

- Is the amount of dividend paid consistent with the company's dividend policy?
- What is the amount of the dividend payment and dividend yield in comparison with the companies in the peer group?
- What is the relationship between the dividend payment and the cash position?
- What is the relationship between the dividend payment and the possible purchase of own shares?
- Has it been made transparent why part of the profit is being allocated to the creation of reserves and what part is ultimately being allocated to the shareholders through the payment of dividend or through the purchase of own shares, and how consistent this is with the company's strategy?

### **I.2.6 Granting discharge to members of the management board and members of the supervisory board**

This is a voting item at the general meeting. The consequence of granting discharge to members of the management board and members of the supervisory board is that the general meeting cannot reconsider components of the policy and supervision at a later time, with the exception of matters that were concealed, were not apparent or not disclosed, or were deliberately misleading. The withholding of discharge is held to be a corrective gesture. This item on the agenda has recently been "used" more often to express dissatisfaction with the policy being pursued, without (immediately) having to submit a motion of no confidence in the management board and/or the supervisory board.

The following are points of reference in this context:

- Is legal action still pending against the company, a member of the management board or a member of the supervisory board?
- If the financial statements are not adopted, granting discharge to members of the management board and members of the supervisory board is not an obvious course of action.
- Has the management board responded adequately in the previous financial year to the remarks of the shareholders with regard to the strategy and policy of the management board? Has the supervisory board played a good, mediating role in this context?
- Has the management board of the company responded adequately to the recommendations made by shareholders in previous general meetings?
- Is the degree of compliance with the Dutch corporate governance code sufficiently high, or have reasons that are acceptable from the perspective of institutional investors been provided for the non-compliances with the provisions of the code?

### **I.2.7 Appointment of members of the management board**

This is a voting item at the general meeting of the listed companies that are not 'structure' companies (*structuurvennootschappen*). At structure companies, members of the management board are appointed by the supervisory board. At the listed companies that do not have to apply the structure regime (*structuurregime*), extra requirements contained in the articles of association can apply to a resolution of the general meeting (e.g. a binding nomination, a qualified majority of votes, a stipulated quorum) to reject the nomination for the appointment of a member of the management board. If the candidate in question is rejected by the general meeting, a new nomination should be presented in a new general meeting and may be expected to have taken the sentiment of the general meeting into account.

The following are points of reference for this item on the agenda:

- What is the quality of the candidate; how does his resumé look?
- What is the service record of the person in question at his previous employer(s) and/or – if applicable – as a member of the supervisory board of another company, also where interacting with shareholders is concerned?
- Are there reasons to doubt the integrity and reliability of the candidate in question?
- Is the candidate in question in keeping with the objective of more quality and diversity in the membership of the management board?
- Is the member of the management board being appointed for a period of four years, in compliance with best practice provision II.1.1 of the Dutch corporate governance code?
- Does the person in question hold more than two supervisory positions with large Dutch or non-Dutch companies or acts as chairman of a supervisory board/board of directors of a large Dutch or non-Dutch company. Is his or her remuneration package in line with the remuneration policy adopted by the general meeting and has the company taken into account the Eumedion principles for a sound remuneration policy for members of the management board of Dutch listed companies (appendix I)?
- In the case of a reappointment, has the supervisory board evaluated the previous period of the appointment and what are the results of this evaluation?

### **I.2.8 Appointment of a member of the supervisory board**

This is a voting item at the general meeting. The general meeting of structure companies can reject the candidate in question by a simple majority of votes<sup>5</sup> representing at least one-third of the issued capital. At the listed companies which do not apply the structure regime, extra requirements contained in the articles of association can apply to a resolution of the general meeting (e.g. a binding nomination,

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<sup>5</sup> This is: the majority of the votes cast plus 1.

qualified majority of votes<sup>6</sup>, a stipulated quorum<sup>7</sup>) to reject the nomination for the appointment of a member of the supervisory board. If the candidate in question is rejected by the general meeting, a new nomination should be presented in a new general meeting and may be expected to have taken the feelings of the general meeting into account.

The following are points of reference for this item on the agenda:

- What is the quality of the candidate; how does his resumé look?
- What is service record of the person in question with his employer and/or – if applicable – as a member of the supervisory board of another company or other companies, also where interacting with shareholders is concerned?
- Are there reasons to doubt the integrity and reliability of the candidate in question?
- Is the member of the supervisory board being appointed for a period of four years, in compliance with best practice provision III.3.5 of the Dutch corporate governance code?
- Has the company provided convincing arguments that the person in questions fits the supervisory board profile?
- Has the company provided meaningful information on the recruitment process (such as the development of selection criteria), the nominated candidate's background, competencies and skill-sets and how they complement the existing supervisory board?
- Is the candidate in question in keeping with the objective of more quality and diversity in the membership of the supervisory board?
- Does the candidate in question have sufficient time to fulfil its role in the supervisory board?
- Does the person in question hold more than five supervisory positions with large Dutch or non-Dutch companies, for which purpose the chairmanship of a supervisory board/board of directors counts double? After the appointment of the person in question, does the supervisory board comply with what is stated in best practice provision III.2.1 of the Dutch corporate governance code (no more than one non-independent member on the supervisory board)?
- In the case of a reappointment, has the supervisory board evaluated the previous period of the appointment and what are the results of this evaluation?
- In the case of a reappointment, does the person in question comply with what is stated in best practice provision III.3.5 of the Dutch corporate governance code (maximum of two reappointments)?
- In the case of a reappointment, was the person in question frequently enough present at the meetings of the supervisory board? Did the company provide detailed information on the presence of the person in question at supervisory board and committee meetings?

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<sup>6</sup> A higher voting majority than 50% plus 1, like two third of the votes cast or 75% of the votes cast.

<sup>7</sup> A specified part of the issued capital that needs to be represented at the general meeting in order to take legally valid decisions.

### **I.2.9 Adoption remuneration policy for the management board and approval of option and share schemes**

#### **a. Adoption of the remuneration policy for the management board**

This is a voting item at the general meeting. The general meeting can put forward changes to the proposed remuneration policy. In practice, the draft then has to go back to the supervisory board, a new meeting may have to be convened and another vote will have to taken.

#### **b. Approval of option and share schemes**

This is a voting item at the general meeting. The general meeting cannot effect any changes to the option and share schemes. The consequence of rejection is, however, that the draft scheme has to go back to the supervisory board, which submits a new scheme to the general meeting for its approval. The previous remuneration policy adopted by the general meeting and/or the share and/or option scheme approved by the general meeting continues to apply in the interim.

The following are points of reference with regard to this item on the agenda:

- Has the company taken into account the Eumedion principles for a sound remuneration policy for members of the management board of Dutch listed companies (Appendix I)?
- Are the provisions of the Dutch corporate governance code with regard to the remuneration of members of the management board (paragraph II.2) being applied to a sufficient extent and/or are arguments that are acceptable to institutional investors provided for non-compliance with the provisions of the code?

### **I.2.10 Adoption of the remuneration for the supervisory board**

This is a voting item at the general meeting. The general meeting can put forward changes to the proposed remuneration. In practice, the draft then has to go back to the supervisory board, a new meeting may have to be convened and another vote will have to taken.

The following are points of reference with regard to this item on the agenda:

- Are the provisions of the Dutch corporate governance code with regard to the remuneration of members of the management board (paragraph III.7) being applied to a sufficient extent and/or are arguments that are acceptable to institutional investors provided for non-compliance with the provisions of the code?
- Has the company provided good reasons for a proposed change in the remuneration of the members of the supervisory board?

### **I.2.11 Proposal to amend the articles of association**

This is a voting item at the general meeting. On the grounds of the articles of association, qualified majorities of votes may apply to some amendments.

The following are points of reference with regard to this item on the agenda:

- Has the company provided good reasons for the proposed amendment to the articles of association?
- If the amendment to the articles of association relates to the curtailment of the existing rights of ordinary shareholders, it would seem logical to vote against the amendment.
- If the amendment relates to a widening of the powers of shareholders, it would seem logical to vote in favour of the proposal.
- If the amendment relates to improved application of the Dutch corporate governance code by the company, it would seem logical to vote in favour.
- The situation is complicated when a number of amendments have been submitted with conflicting implications for shareholders' rights. In that event, it is always possible to request unbundling of the proposals (this is also recommended in best practice provision IV.3.9 of the Dutch corporate governance code).

### **I.2.12 Appointment statutory auditor**

This is a voting item at the general meeting.

The following are points of reference with regard to this item on the agenda:

- Is it transparent what task assignment the supervisory board wants to give to the statutory auditor?
- Has the supervisory board prepared a transparent and comparative cost analysis of audit firms that are qualified for the task assignment?
- In the event of a change of statutory auditor that is not prompted by the statutory obligation to change the statutory auditor, has the company provided good reasons for this change?
- Has the supervisory board made a thorough assessment of the functioning of the present statutory auditor and what are the most significant conclusions of this evaluation?
- What is the track record of the statutory auditor and of the firm where he is employed?
- Does the firm where the statutory auditor is employed have a licence from the AFM?
- Are there reasons for doubting the integrity and reliability of the organization where the statutory auditor is employed?
- What is the proportion of the amount that the company pays for the audit tasks carried out by the statutory auditor in relation to that for non-auditing tasks carried out by the same firm where the statutory auditor is employed?

- Has the company taken into account the Eumedion guidance for the explanatory notes to the nomination for (re)appointment of the statutory auditor (see Appendix IV)?

### **I.2.13 Delegation of power to issue ordinary and preference shares**

This is a voting item at the general meeting.

The following are points of reference with regard to this item on the agenda:

- Has the company taken into account the Eumedion recommendations concerning the delegation of the power to issue shares (see Appendix II)?

### **I.2.14 Authorization of the management board to repurchase own shares**

This is a voting item at the general meeting. Authorization cannot be given if the financial statements have not been adopted.

The following are points of reference with regard to this item on the agenda:

- Has the company taken into account the Eumedion recommendations concerning the authorization to repurchase own shares (see Appendix III)?

### **I.2.15 Approval major transactions**

This is a voting item at the general meeting.

The following are points of reference with regard to this item on the agenda:

- Has the management board demonstrated convincingly how the interest of the (minority) shareholders has been weighed against other interests?
- In the event of a takeover, is this takeover consistent with company strategy? Have the risks associated with the takeover been made sufficiently transparent?
- In the event of a takeover, has it been demonstrated convincingly that the advantages of the synergy are greater than the cost price of the takeover, taking what are known as the integration costs into account and the costs of financing the takeover? Is it possible to express the projected synergy benefits in concrete figures with a corresponding concrete time frame? Has the management board submitted a convincing implementation process to the general meeting, complete with scenarios and evaluation moments?
- In the event of a takeover, is the management board able to indicate how the takeover price was reached? Has a transparent fairness opinion been issued by a bank that is not involved in the transaction or accountancy firm, providing information on the prognoses assumed for the company being taken over? Have fairness opinions been issued that have not been published?

- In the event of a division or participating interest being disposed of, has it been demonstrated convincingly that the maximum feasible price has been stipulated?
- How does the takeover/disposal fit in with the company's long-term strategy?

#### **I.2.16 Shareholders' proposals**

A subject submitted by one or more shareholders who have made use of the right to place an item on the agenda can be put forward for discussion or put to a vote. The vote on the shareholders' proposal may be binding or non-binding in nature. The vote is binding if the proposal relates to a field which is within the powers of the general meeting on the grounds of the law or articles of association. The vote is not binding in all other cases, but the result of the vote does send a signal to the management board and the supervisory board. An opinion on a shareholders' proposal should be formed on the merits of each individual case, in which process the reference points listed above for the items on the agenda can be taken into consideration.

## **SECTION II: SHAREHOLDERS' RESPONSIBILITIES IN THE NETHERLANDS**

## II.1 Summary of the responsibilities of (certain) shareholders

The number of shareholders' rights has been extended in the last few years. Shareholders have the task of dealing responsibly with these powers and they have recently been increasingly reminded of this responsibility. The following obligations and rules of conduct for shareholders can be distilled from legislation and regulations, the Dutch corporate governance code, and from the jurisprudence.

### *Transparency*

- a) statutory obligation to immediately report the acquisition or disposal of shares if certain threshold values of the issued capital and/or voting rights<sup>8</sup> are exceeded or fallen short of (5, 10, 15, 20, 25, 30, 50, 75 and 95%)<sup>9</sup> (section 5:38 par. 3 and 5:39 par. 2 Financial Supervision Act [Netherlands]);
- b) statutory obligation to report a net short position in the issued capital of a company whose shares are admitted to trading on a trading platform to the public supervisor on each occasion that the position reaches the threshold of 0.2% of the issued capital of the company concerned and on each occasion that it reaches 0.1% above this level (article 5 Short Selling Regulation). A net short position of at least 0.5% of the issued capital will be publicly disclosed by the public supervisor (article 6 Short Selling Regulation).
- c) a shareholder who exercises the right of putting an item on the agenda of a general meeting is required to be transparent on his full economic interest ('long' and 'short') in that company at the time of exercising this right (section 5:25k bis Financial Supervision Act [Netherlands]);
- d) institutional investors annually publish, on their website at least, their policy on the exercise of voting rights on shares that they hold in listed companies (best practice provision IV.4.1 of the Dutch corporate governance code)<sup>10</sup>;
- e) institutional investors report annually on their website and/or in their annual report on the implementation of their policy on the exercise of voting rights in the relevant financial year (best practice provision IV.4.2 of the Dutch corporate governance code);
- f) institutional investors report at least once a quarter on their website, whether and how they have voted as shareholders at the general meetings (best practice provision IV.4.3 of the Dutch corporate governance code).

### *Best practices in dealing with the company and fellow shareholders*

- a) shareholders shall act in relation to the company, the organs of the company and their fellow shareholders in keeping with the principle of reasonableness and fairness. This includes the

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<sup>8</sup> Including economic long positions like contracts for difference, cash-settled equity swaps, total return equity swaps, cash-settled call options and the selling of put options.

<sup>9</sup> The Act on amending the Financial Supervision Act, the Securities (Bank Giro Transactions) Act and the Civil Code in response to the advice of 30 May 2007 from the Corporate Governance Code Monitoring Committee introduces an additional threshold value at 3% of the issued capital or voting rights. Another element of this Act is the requirement for an investor to disclose his gross short position in a share of a Dutch listed company provided that this is a value of at least 3% of the issued capital. The Act will enter into force on 1 July 2013.

<sup>10</sup> Paragraphs c, d and e have a legal basis for Dutch institutional investors in the Financial Supervision Act, whereby the "apply or explain" rule applies.

willingness to engage in dialogue with the company and their fellow shareholders (principle IV.4. of the Dutch corporate governance code).

- b) a shareholder with a large block of shares should, on the grounds of reasonableness and fairness, make disclosure to and consult reasonably with the company in question. In this context, he will have to disclose whether the block acquired is for investment purposes only, or whether he wishes to exercise influence on company policy with the block acquired (and wishes a seat on the management board or on the supervisory board to that end), or whether the interest acquired is the basis for the acquisition of a majority interest which is intended in turn to lead to acquisition of absolute control of the company. The company in question has an obligation to take note of the intentions of the shareholder and to investigate these intentions (jurisprudence<sup>11</sup>).
- c) shareholder and target company are subsequently obliged to consult together (jurisprudence<sup>12</sup>).
- d) the general meeting can express its ideas on strategy by exercising the rights assigned to it in law and in the articles of association. The general meeting must take reasonableness and fairness into consideration in exercising these rights (jurisprudence<sup>13</sup>).
- e) if a major shareholder is not in agreement with the policy or strategy of the company, he must present credible alternatives and consult with the management board on this subject. If this does not happen, a policy change that a major shareholder wishes to implement is too much of a risk for other interested parties, such as employees and minority shareholders (jurisprudence<sup>14</sup>).
- f) shareholders take careful note and make a thorough assessment of the reasons given by the company for any non-application of the best practice provisions of the Dutch corporate governance code. They should avoid adopting a 'box-ticking approach' when assessing the corporate governance structure of a company and should be prepared to enter into a dialogue if they do not accept the company's explanation. There should be recognition that corporate governance must be tailored to the company-specific situation and that non-compliance of individual provisions by a company may be justified (principle I of the Dutch corporate governance code).
- g) a shareholder shall exercise the right of putting an item on the agenda of a general meeting only after he consulted the management board about this. If one or more shareholders intend to request that an item be put on the agenda that may result in a change in the company's strategy, for example through the dismissal of one or more management or supervisory board members, the management board shall be given the opportunity to stipulate a reasonable period in which to respond (the response time). This shall also apply to an intention as referred to above for judicial leave to call a general meeting pursuant to section 2:110 Civil Code. The shareholder shall respect

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<sup>11</sup> Amsterdam Court of Appeal (Enterprise Section) 11 March 1999, JOR 1999, 89 (Breevast), grounds 4.16 and Amsterdam Court of Appeal (Enterprise Section) 22 March 2002, JOR 2002, 82 (Rodamco North America), grounds 3.8 and 3.9.

<sup>12</sup> Amsterdam Court of Appeal (Enterprise Section) 8 March 2001, JOR 2001, 55 (Gucci).

<sup>13</sup> Amsterdam Court of Appeal (Enterprise Section) 17 January 2007, JOR 2007, 42 (Stork) and Netherlands Supreme Court 13 July 2007, NJ 2007, 434 (ABN AMRO Holding and 9 July 2010 (ASMI)).

<sup>14</sup> Amsterdam Court of Appeal (Enterprise Section) 17 January 2007, JOR 2007, 42 (Stork).

the response time stipulated by the management board and that is maximised at 180 days (best practice provision IV.4.4 of the Dutch corporate governance code)<sup>15</sup>.

- h) if a shareholder has arranged for an item to be put on the agenda, he shall explain this at the meeting and, if necessary, answer questions about it (best practice provision IV.4.6 of the Dutch corporate governance code).
- i) a shareholder shall vote as he sees fit. A shareholder who makes use of the voting advice of a third party is expected to form his own judgement on the voting policy of this adviser and the voting advice provided by him (best practice provision IV.4.5 of the Dutch corporate governance code).
- j) if a shareholder or a group of shareholders acting in concert acquires at least 30% of the voting rights, an obligation comes into effect to issue a public offer for all shares in the company (section 5:70 in conjunction with 1:1 Financial Supervision Act [Netherlands]);
- k) as from 1 January 2013 all financial institutions in the Netherlands – including pension funds – will be prohibited from investing in companies that manufacture, sell or distribute cluster ammunition. The ban is limited to new investments; existing investments should be divested within a “reasonable period” (draft article 21a of the Market Abuse Decree).

In addition to the above, the principle of Dutch corporate law also applies; that the exercise of rights and obligations can be evaluated in the light of the behavioural standard of reasonableness and fairness (section 2:8 Civil Code). This standard will be achieved more quickly when the influence of the investor is greater, because he has a relatively large block of shares in a company for example. There are also other specific situations in which the shareholder cannot entirely serve his own interests when exercising his voting rights. This applies, for example, in the situation where the shareholder does not hold the share interest in the relevant company for financial purposes alone, since other interests are also involved. The shareholder might be a competitor of the company, for instance, or the shareholder may have a direct interest in a transaction with the company. This shareholder must act reasonably and fairly in the exercise of his rights, from which it follows that he must always take the possible consequences of his voting behaviour on the continuity of the business operations into consideration when deciding whether to vote for or against a proposal.

## **II.2 Eumedion Best practices for engaged share-ownership**

On 30 June 2011 Eumedion adopted a set of ten best practices for engaged share-ownership, intended for Eumedion participants. It is expected of the Eumedion participants that they observe the ‘apply or explain’ rule for these best practices, just as they do with the Dutch corporate governance code. The best practices are incorporated in their entirety in Appendix V.

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<sup>15</sup> Paragraphs g, h and i have a legal basis for Dutch institutional investors in the Financial Supervision Act, whereby the “apply or explain” rule applies.

### **II.3 Securities lending**

It frequently occurs that institutional investors legally transfer (a quantity of their) shares to a party that must transfer these shares in the near future for a variety of reasons; this is also referred to as *securities lending*. The recipient undertakes at the same time to transfer back an equal number of the same shares at a later time, subject to the payment of a lending fee. The practice of securities lending leads to a dilemma where corporate governance is concerned. The institutional investor will have to balance the amount of the lending fee that can be earned to the benefit of its beneficiaries, against the benefits of voting at the general meeting. Securities lending could be detrimental to the goal of increasing the participation of shareholders in the decision-making process at general meetings and consequently of voting as many shares as possible. It is not enforceable that - nor is it verifiable in practice whether and how - the recipient exercises the voting rights on the borrowed shares. It is extremely possible that the parties who have borrowed the shares exercise the voting rights in a manner that is diametrically opposed to the voting policy of the institutional investor who is the beneficial owner of the shares. This is not in keeping with the fiduciary responsibility of the institutional investor to (also) manage the controlling rights attached to shares in a correct and responsible manner.

In its evaluation of the 2006 proxy season, Eumedion took the stance that the lending of shares by institutional investors in event-driven situations affecting the listed company should be discouraged. If a certain general meeting can result in an event-driven situation of this kind, Eumedion will bring this to the attention of its members and will suggest that the members consider recalling any lent shares before the registration date that applies to this general meeting.

Furthermore, Eumedion supports the Securities Lending Code of the ICGN, which was published in July 2007 and sums up the points for attention for institutional investors with regard to securities lending. The Securities Lending Code is incorporated in full in this document as Appendix VI.

### **II.4 Cooperation with other shareholders (acting in concert)**

#### **II.4.1 Compulsory notification of a substantial interest in a Dutch listed company**

Shareholders are becoming increasingly more active and are making increasing use of their shareholders' rights. Institutional investors who take their role as active shareholders seriously can make contact with each other and generally do so with the objective of sharing information and research efforts. In certain circumstances, however, close cooperation between shareholders can lead to an obligation to notify on the grounds of section 5:45, par. 5 Financial Supervision Act [Netherlands]). This section stipulates that a person is deemed to have the disposal of the votes of which a third party has the disposal, if it has concluded a (verbal or written) agreement with this third party that provides for a "long-term common policy" on casting votes (for a longer period, in any event, than a single general meeting); this is also referred to as acting in concert. This is what is known as a notification of a

substantial unit, on the grounds of which shareholders must notify the AFM when certain of the threshold values referred to in chapter 5.3 Financial Supervision Act [Netherlands] have been reached/fallen below. The minimum threshold for notification has presently been set at least 5% of the issued capital or votes in a listed company<sup>16</sup>. The consequence of the notification is that the notification is included in a register that can be inspected by the general public. It is important for institutional investors to know when cooperation is so close that it is held to be acting in concert. The situations in which acting in concert exists must be clear in order to prevent institutional investors from rightly (but possibly wrongly as well) being faced with negative publicity or confronted with sanctions under administrative law and/or civil law, in the event of non-compliance with the notification rules<sup>17</sup>.

In November 2009 the AFM issued the following guidance relating to the question of when acting in concert exists in the sense of chapter 5.3 of the Financial Supervision Act [Netherlands]:

### **“Consultation**

The AFM believes that consultation between shareholders can help increase the level of insight into the corporate governance of an issuer. This consultation can help shareholders convey their views to an issuer more effectively and clearly. This applies in particular with a view to preparations for a general meeting of shareholders, whereby consultation can lead to the granting of proxies and voting instructions. Such forms of consultation are generally not based on an agreement to pursue a *sustained* joint voting policy and therefore do not qualify as ‘acting in concert’.

As regards ‘acting in concert’ the AFM provides the following guidelines.

#### **Agreement concerning sustained joint voting policy**

If an agreement has been concluded between the parties that obliges them to pursue a sustained joint policy and to exercise their voting right jointly, each individual party will be considered to have disposal of the voting rights disposed of by the other party. In other words, as long as each party concerned retains the freedom to exercise its voting right independently (or have its voting right exercised) – at its own discretion – a sustained joint voting policy will not exist.

A sustained policy does exist if the agreement, which may have been entered into verbally or in writing, does not apply for just one general meeting of shareholders. The agreement can also be concluded by, for example, a handshake, on the basis of which the parties in question can mutually deduce that they will exercise their voting right in a certain way at a number of general meetings of shareholders.

The AFM will not always know whether an agreement has been made to pursue a sustained joint voting policy. The AFM may believe there is cause to request information from the parties in question if the cooperation is oriented around a subject that can lead to a change in the issuer's strategy, for example by jointly nominating one or more directors or supervisory directors.

Various facts and circumstances may cause the AFM to suspect the existence of an agreement to pursue a sustained joint voting policy. The AFM can request information from the parties that are presumed to be cooperating on a strategic issue if, in the run-up to, during, or after a

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<sup>16</sup> See however footnote 9.

<sup>17</sup> Under administrative law means that the AFM can impose a fine or a penalty and can publish this fact. Under civil law means that other interested parties (other shareholders, the company) can apply to a court to compel the person subject to the notification obligation to make the notification now, to suspend the exercise of voting rights, to suspend the implementation of resolutions passed at the shareholders' meeting, or to annul these resolutions.

general meeting of shareholders, a number, but not necessarily all, of the following facts or circumstances occur:

- The parties use the same lawyer or legal advisor.
- The parties send the issuer letters with the same purport.
- The parties jointly initiate (legal) proceedings.
- The parties jointly approach the issuer.
- The actual voting behaviour of the parties at the general meetings of shareholders is repeatedly similar.
- The parties have mutually issued or received instructions relating to behaviour or voting.
- A decision relating to a strategic issue is added, on the initiative of the shareholders, to the agenda of a general meeting of shareholders.
- The shareholders have agreed fees or guarantees.
- The parties are established at the same address (as given in the articles of association).
- The parties publicly announce that they are collaborating.
- The purchasing/selling behaviour of affiliated parties, for example a (legal) entity bound in a formal or actual control structure, a (legal) entity which can directly or indirectly exercise a voting right or can exercise certain rights in some other way as a result of which significant influence can be exerted on the commercial or financial policy or a related natural person.

This summary of facts and circumstances is not exhaustive.”

#### **II.4.2 Obligation to make a public offer for the shares of a Dutch limited company**

On the grounds of section 5:70 Financial Supervision Act [Netherlands], a party that has acquired overall control is obliged to issue a public offer. Overall control exists when a party (alone or jointly with persons acting in concert with it) can exercise 30% or more of the voting rights. The objective of acting in concert must be either (i) to acquire overall control, or (ii) to cooperate with the target company to thwart an offer that has been announced. The acting in concert does not have to be evidenced by a written agreement. Verbal agreements, and even tacitly understood actions, may suffice. The law assumes that acting in concert always applies in certain relationships e.g. if shares are held by distinct group companies, spouses, or relations by blood or affinity. The existence of acting in concert depends on the circumstances of the case and will depend on the objective of the cooperation. The Netherlands Minister of Justice made the following comments in this connection during the parliamentary debate on the bill to introduce the compulsory bid into Dutch legislation and regulations “When cooperation takes place with a view to the adoption of joint stances on the principles of the corporate governance of a company, the acquisition of overall control will generally be absent as a goal in this process [...]. It can be stated in clarification that cooperation with the intention of achieving overall control will generally also not be involved if the cooperation and exchange of information between shareholders on the subject of the corporate governance of a company relates to a more effective decision-making process in the shareholders’ meeting or to stimulate dialogue with the company. In other words, an effective dialogue between (a group of) shareholders and company management can take place, therefore, without the obligation to issue a public offer arising, to the extent that those engaged in this dialogue do not have the objective of acquiring overall control”<sup>18</sup>. The legislator has provided no concrete

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<sup>18</sup> Parliamentary Papers (Netherlands) I 2006/07, 30 419, no. C.

indications, however, as to what is still classified as corporate governance and when the will exists to exercise overall control. The AFM has no role in the interpretation of the concept of persons acting in concert within the context of the compulsory bid. It is left to the Enterprise Section of the Court of Appeal in Amsterdam and ultimately to the European court to interpret this concept.

### **SECTION III: PRACTICAL MATTERS**

### **III.1 Practical matters with regard to the exercise of voting rights**

In view of the international spread of the investment portfolios of institutional investors, it is impracticable in most cases to attend all shareholders' meetings. In order to vote, therefore, institutional investors will mostly give a proxy to a third party. This third party may be anyone, although in practice it is usually an asset manager, a custodian, a specialized party (a corporate governance service provider, for example, or a depository or trust office), a fellow shareholder, or the notary of the general meeting.

The proxy may be "open", which implies that the proxy-holder himself may decide how he votes, or "closed", which means that the proxy-holder has been instructed in advance on how to vote. Casting votes in this way is known as proxy voting and is a form of "distance voting". Other forms are voting by post or by internet, i.e. *e-voting*, which is increasingly being offered. A number of these options are listed below.

#### **III.1.1 Granting a proxy to a Eumedion member who is attending the general meeting of the listed company in question**

Eumedion members can give a proxy to the Eumedion member who is "physically" attending the general meeting of the relevant company. Approximately one month and a half before the AGM season, Eumedion circulates an overview of the Dutch shareholder meetings at which a Eumedion member will be present who is willing to take voting proxies from other Eumedion members to the meeting. The following procedure has been agreed.

1. As soon as the name and identity details of the person from the Eumedion member who is going to attend the general meeting are known, it is advisable for members to notify their own custodians accordingly. This can sometimes be done electronically by means of what is known as a voting platform. It can be indicated via a system of this kind that the shares in question will be "physically" voted, i.e. during the general meeting, and the contact details of the person who is actually going to be voting should be provided filled in at this time. Members who do not use a voting platform of this kind should send this information (physical voting and by whom) to the custodian bank and a member of the bank staff will then complete the necessary paperwork<sup>19</sup>.
2. The member receives a certificate of deposit from the custodian and this serves as an admission ticket for the general meeting in question. The certificate states the name of the beneficial owner of the shares, the number of shares held by the beneficial owner on the registration date, and the name of the person to whom the proxy has been given. The bank or the investor usually has to sign the certificate of deposit in order to have actual access to the shareholders' meeting.
3. The person attending the relevant general meeting should be informed that he is being granted a proxy to vote and/or speak on behalf of the member in question. This person will ensure that the

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<sup>19</sup> It is advisable, however, to apply directly to the custodian for a proxy form, in order to save time and avoid the risk of something going wrong in the voting chain.

analysis of the items on the agenda to be dealt with and the recommended voting behaviour are circulated in good time before the general meeting.

4. As soon as the draft certificate of deposit has been received from the custodian, it is recommended to forward this draft to the person who will actually be attending the general meeting, so that he knows in good time on whose behalf he is going to vote (in addition) and approximately how many votes he will be representing.
5. The final certificate of deposit should be sent to the person receiving the proxy (preferably by fax or e-mail). This is done by either the custodian or by hand by the member (if his signature is required on the proxy, for example). The person attending the general meeting in question should take this certificate of deposit to the meeting with him, as proof that he is also voting on behalf of that other party.
6. As soon as the granter of the proxy has studied the draft analysis of the items on the agenda and the recommended voting behaviour and has decided whether or not to follow the advice, the proxy holder must be informed accordingly. It is possible for the proxy holder to vote differently on different proxies at the general meeting.
7. It is advisable for the granter of the proxy to make contact with the company in question one or two days before the shareholders' meeting, in order to ensure that the company has received the same information and that the completed forms meet the stipulated requirements.
8. It is advisable for the person who is physically attending the shareholders' meeting to be present at least one hour before the meeting starts, so that he is sure of having sufficient time to complete the verification procedures. The person should have valid proof of identity with him. It has proved useful to keep the names and (mobile) telephone numbers of the custodian(s) involved, the company secretary and the investors represented ready to hand.

### **III.1.2 Shareholders Communication Channel**

The 2000 AGM season saw the first opportunity to vote by proxy in the Netherlands using the Shareholders Communication Channel [Stichting Communicatiekanaal Aandeelhouders]. This communications channel offers shareholders a convenient and efficient method of casting their votes. In formal terms, they give the proxy to a central proxy-holder, who votes on their behalf during the meeting. The central proxy-holder has no independent will; he collects proxies and votes automatically in accordance with specific instructions. In essence, therefore, this is actually a form of "remote voting", i.e. without being physically present at the shareholders' meeting.

The communications channel has its limitations, however, one of which is that only a small number of companies participate. The second is that only holders of Dutch securities accounts are reached in practice. These are private individuals, therefore, who hold a securities account with one of the participating Dutch banks, but institutional investors who hold an account with a non-Dutch custodian

cannot vote through the communications channel in practice, or only with difficulty. The reason for this is the largely virgin territory of ownership rights to securities in international chains of intermediaries.

### **III.1.3 International practice**

The share portfolio of an institutional investor will, for the most part, consist of non-Dutch companies. The custodians (banks) of an institutional investor will generally have a working relationship with an international voting service. Institutional investors who wish to exercise their voting rights attaching to these non-Dutch shares can do so by using the internet options offered by the international voting service providers and it is thereafter the custodian's responsibility as authorized agent to ensure that the vote actually reaches the company.

It is not only possible to cast votes using the internet facilities, but voting advice for each item on the agenda can also be obtained through the consultancy where the institutional investor is a client. An institutional investor is able to outsource much of the voting process in this way, while still efficiently making a well-considered vote count. This does not alter the fact that the institutional investor remains responsible for the voting behaviour and, therefore, for the monitoring of the actual implementation of the voting policy by a third party. As a consequence, the institutional investor will have to decide who is responsible within its own organization for the implementation of the voting policy. It should be borne in mind in this context that decisions have to be made at short notice in many cases, since the period between the publication of the agenda and the registration of the vote cast is a limited one. It should also be realized that voting is largely a seasonal activity that peaks in the March-June period, due to the link between the date of the close of the financial year and the date of the general meeting.

Furthermore, the voting chain is only as strong as its weakest link and all sorts of administrative and legal obstacles remain to exercising voting rights.

The international proxy advisory services offer the following options:

- The proxy advisory service provides an analysis of the items on the agenda with a corresponding voting recommendation. All the client has to do is to monitor the recommendations to decide, for example, whether they are consistent with its own voting policy or with its own voting behaviour guidelines. Once this has been done, the votes can be cast.
- Larger scale outsourcing of the voting process is possible. The consecutive process of receiving the convocation for a general meeting and the voting forms, determining the number of votes that can be cast, casting the votes themselves, and keeping note of how the votes were cast can be transferred in its entirety to the proxy advisory service. The advisory service then votes in accordance with the client's voting behaviour guidelines, or on the basis of the client's voting policy that was communicated in advance.

- A variant on this is the service of alerting the client to the circumstance that specific attention is required for the agenda of a general meeting, but only in the case of a number of shares selected by the client. These are mostly the shares in the companies in the country where the client is established or in companies where controversial matters are at issue.

Institutional investors who work with external asset managers can agree with these asset managers that the latter will exercise the voting rights attaching to the shares in portfolio in accordance with the voting policy formulated by the institutional investor, which can be set out in the management agreement. It will still be necessary, however, for the institutional investor to make certain that this policy is actually being implemented. After all, the institutional investor continues to be responsible at all times for the voting behaviour on the shares.

#### **III.1.4 Proxy solicitation**

Institutional investors with an active interest in corporate governance will not only want to vote themselves, but will also want to be in touch with other shareholders, if necessary, in order to build greater joint voting power by collecting proxies; this is known as proxy solicitation. The Act on implementing the advice of the Corporate Governance Code Monitoring Committee<sup>20</sup> makes it possible for shareholders to send information to fellow shareholders via the listed company. The solicitation of proxies through sending this information is not permitted, however. Where appropriate, Eumedion coordinates members' efforts to this end, when one of the members asks other institutional investors for proxies (see above). The problems of acting in concert should, however, be taken into consideration in this context (see paragraph II.5).

#### **III.1.5 Engagement**

In certain cases, institutional investors wishing to make use of their voting rights need more than their own analyses of the proposals published by the company or the recommendations of specialist proxy advisory services. They will require the company to provide further clarification or an explanation of the proposals before deciding on their voting behaviour and the company will be willing to acquiesce, in principle, in order to minimize the risk of a vote against. The sounding out of proposals in advance of the general meeting prevents the unnecessary polarization of positions in the course of the meeting. In this light, discussions with the management board are consistent with careful preparation of the decision-making process at the general meeting. These discussions can be one on one or group conversations with or on behalf of several shareholders. Moreover, the massive scale and openness of a general meeting does not make this the most appropriate forum for a good and substantive exchange

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<sup>20</sup> The Act on amending the Financial Supervision Act, the Securities (Bank Giro Transactions) Act and the Civil Code in response to the advice of 30 May 2007 from the Corporate Governance Code Monitoring Committee. See also point h) on page 10 of this Manual.

of opinions on company policy and strategy. These are the reasons why institutional investors are increasingly pursuing a dialogue with the company outside the general meeting.

The communication of price-sensitive information should be avoided during the meetings, because price-sensitive information must in fact be provided equally and simultaneously to all investors. If the management board nevertheless (unintentionally) imparts price-sensitive information during the dialogue with (a group of) shareholders, this information will have to be made public as soon as possible by means of a press release, unless the confidentiality of the information is guaranteed because, for example, the recipient of the information is bound by an obligation to observe secrecy<sup>21</sup>. Institutional investors themselves can also take measures to reduce the risk of “accidents”. It is customary to establish in advance that no price-sensitive information will be exchanged, the institutional investor explicitly reserving to itself the right to disclose any price-sensitive information still acquired, should the company fail to do so. It is also advisable for a discussion of this kind to be conducted with at least two people representing the institutional investor. Another institutional investor is sometimes invited to attend the meeting as well, in order to reduce the risks of unilateral distribution of price-sensitive information.

In an interview with one of its (former) management board members in two daily newspapers, the AFM issued some guidance on one-on-one meetings between listed companies and investors:

“According to Maatman, companies have no need to be afraid of the AFM where one-on-one meetings are concerned, unless price-sensitive information is exchanged. ‘You are always allowed to listen to your shareholders. And an executive is always allowed to respond.’ Maatman does advise making a good report of the meeting. ‘The text doesn’t have to be published on the internet and there is no need for a tape either.’ (Financieele Dagblad, 20 November 2009). ‘This does not change the fact that executives must be very cautious about sharing price-sensitive information. You mustn’t take a shareholder by surprise with things like that. And it must be necessary.’ (De Telegraaf, 20 November 2009).

These statements make it clear that the AFM also believes that dialogue between shareholders and enterprises can contribute to better understanding and a restoration of mutual confidence<sup>22</sup>.

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<sup>21</sup> Section 5:59 Financial Supervision Act [Netherlands].

<sup>22</sup> This does not affect the fact that an institutional investor can also decide on the basis of section 5:59 paragraph 5 Financial Supervision Act [Netherlands] to enter into a confidentiality agreement with the management of the company. An institutional investor will not lightly sign an agreement of this kind, incidentally, because an institutional investor is no longer permitted then to trade in shares and other securities of the company to which the inside information refers. A trading restriction of this kind can be (very) expensive and result in conflict with the investment strategy pursued by the institutional investor.

## **SECTION IV: ABOUT EUMEDION**

### ***Good corporate governance***

Pension funds and other major asset managers from all over the world work together in Eumedion in order to better fulfil their role as (co-)owners of Dutch listed companies.

A company is, after all, an alliance of interested parties of all kinds who want to be rewarded for their contributions. In the case of smaller companies, the owner weighs up the particular interests and the owner ultimately decides on company policy. In the case of listed companies, ownership is spread over the shareholders, who want to make their votes count at shareholders' meetings and can also enter into dialogue with company management outside these meetings. Eumedion brings institutional investors together, promotes their interests as shareholders, and furthers good corporate governance.

### ***More than one thousand billion euros***

Eumedion was formed in 2006 and currently has approx. seventy members. More than half of these are Dutch pension funds and the other members are investment funds, insurance companies and other asset managers of mainly Dutch origin. The number of foreign asset managers that are members of Eumedion is substantial now and continues to grow.

The members of Eumedion collectively manage more than one thousand billion euro, which is approximately twice as much as the combined annual earnings of the entire population of the Netherlands. The members of Eumedion collectively hold approximately 20% of the shares in Dutch listed companies.

### ***Joining forces***

Shareholders used to pocket their dividends and sold their shares if they did not like the company policy, but things are different now. Major institutional investors are definitely expected to shoulder their responsibilities as co-owners and Eumedion helps them to do so by ensuring, in the first place, that voting at shareholders' meetings is more efficiently organized.

It is partly thanks to Eumedion, for example, that Dutch listed companies publish their agendas sooner and that investors can make better preparations as a consequence. Eumedion members also often act on behalf of each other at shareholders' meetings, which enables them to make their voices heard in the discussion and to cast their votes as well, without having to attend all the meetings in person. In addition, Eumedion can also make contact with a management board and supervisory board on behalf of the members, in order to communicate issues that are giving rise to concern.

In the Hague and Brussels, Eumedion also guards the interests of institutional investors by keeping a critical eye on developments relating to legislation and regulations and making proposals on how to do

things better. As a representative of institutional investors, Eumedion also participates in various institutions as well, such as the Corporate Governance Code Monitoring Committee and the Dutch Accounting Standards Board.

In this way, Eumedion contributes to good corporate governance and sustainability at listed companies, while saving its members time and money.

### ***Policy and implementation***

Eumedion regularly commissions research into issues of current interest in the field of corporate governance and sustainability, such as the remuneration policy for corporate executives, and also takes part in the public debate by means of a wide range of publications and press releases. The annual symposium is always a highlight in this context, above all because the members debate the issues directly with each other. In addition, Eumedion has five committees that focus on subfields such as legislation, financial reporting, shareholders' meetings and the dialogue with companies. The members of these committees are also able, on Eumedion's behalf, to enter into dialogue with legislators, for example, or with representatives of other interested parties. The executive director of Eumedion and his staff organize all processes and ensure that these proceed smoothly. Eumedion also has a General Board consisting of members' representatives. The General Board decides on policy and chooses an Executive Board from among its members to supervise the implementation of policy. The General Board is accountable to the Members' Meeting that takes place twice a year.

### ***Contact***

You will find more information about Eumedion on the website at [www.eumedion.nl](http://www.eumedion.nl) where you will also find all publications, such as research reports, opinions and press releases. And you can, of course, also contact Eumedion.

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## **Appendix I: Eumedion principles for a sound remuneration policy for members of the management board of Dutch listed companies**

### *Background*

The tasks of the management board, the supervisory board and the general meeting are clearly distinguished in Dutch corporate law. The management board manages the company; the supervisory board supervises and advises the management board, and the general meeting monitors both the management board and the supervisory board. Shareholders are not intended to act the part of members of the management board, or to act the part of the supervisory directors.

The division of tasks is different, however, where the remuneration of management board members is concerned. The management board determines directly or indirectly the remuneration of all the other employees of the company, but it is obviously undesirable for the members of the management board to determine their own remuneration. As a consequence, supervisory directors have been given a more executive task with regard to the remuneration of directors under the articles of association which means that the task of the general meeting has altered as well. In the case of the remuneration of the management board, the supervisory board initiates and implements the policy here and the general meeting monitors the way in which the supervisory directors do this.

The legislator gave an explicit shape to this special role allocation with respect to the remuneration of members of the management board with effect from 1 October 2004. As from that date, the general meeting has had the right to determine the remuneration policy for management board members and the right to approve schemes in the form of shares or rights to subscribe for shares. According to the law, the general meeting also determines the remuneration of individual management board members, but it is permitted for the articles of association to designate another body to perform this task. This latter option is mostly used at listed companies with a widely dispersed shareownership. Determination of the remuneration of individual management board members at such companies has mostly been transferred to the supervisory board or to the meeting of holders of priority shares, which implements policy in this regard.

This means, in practice, that the general meeting only adopts the remuneration policy for management board members at listed companies on the recommendation of the supervisory board, and the policy is subsequently implemented by the supervisory board. As is stated in principle II of the Dutch Corporate Governance Code: “The supervisory board shall determine the remuneration of the individual members of the management board, on a proposal by the remuneration committee, within the scope of the remuneration policy adopted by the general meeting.” Under the law, the results of that policy – the total remuneration paid to individual management board members broken down into its various components

– should be presented in the explanatory notes to the annual report. In this way, the general meeting is enabled to monitor the implementation of the policy by the supervisory board.

This supervisory role of the general meeting comprises a number of elements, therefore. It involves the adoption (in advance) of a proposal for a remuneration policy for the management board, the adoption (in advance) of any amendments to this policy, the approval (in advance) of schemes in the form of shares or rights to subscribe for shares, the approval (in advance) of any changes to these schemes, and the evaluation (in retrospect) of the results of the policy, as these are formulated in the remuneration report from the supervisory board that is part of the annual report (best practice provision II.2.12 in conjunction with III.1.2 of the Dutch Corporate Governance Code).

Eumedion has drawn up the principles for a sound remuneration policy set out below in order to support Dutch and international shareholders in the listed companies with statutory seat in the Netherlands<sup>23</sup> in the supervisory task assigned to them by the law and the Dutch Corporate Governance Code with respect to the remuneration of management board members. These principles relate to the process and the accountability, as well as to the structure and content of a sound remuneration policy.

The principles set out below build on the 2006 Eumedion recommendations on executive remuneration and on the provisions contained in the revised Dutch Corporate Governance Code of December 2008. They go further, however, on a number of points, such as principles 8 en 9, because it had not been possible for the revised Dutch Corporate Governance Code to take sufficient account of the recent conclusions reached in the national and international discussion on sound remuneration policies. In these new principles Eumedion emphatically endorses the mandate of the supervisory board to fashion a suitable remuneration policy for the management board, but this does not diminish in any way the power of the general meeting with regard to adopting the policy. More emphasis will be placed on adequate accountability in retrospect for the policy adopted in advance and the scope this implies, so that the general meeting can monitor implementation of the remuneration policy. This will be found in principles 4 and 5 for example, which include recommendations that follow on from the existing legal regulations in the United Kingdom and the United States, stipulating that the report on the implementation of the remuneration policy for the relevant financial year (the remuneration report) must be put to a vote at the general meeting. It is also recommended to evaluate the remuneration policy as a whole at least once every four years and to allow the general meeting to decide on the continuation of this policy or the amendments to it. Moreover, it is recommended to not only base any variable remuneration elements on financial, but also on environmental, social and/or governance objectives.

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<sup>23</sup> Since the scope of Eumedion's work is confined to the corporate governance and sustainability issues at Dutch listed companies, the principles in this document relate solely to that group of companies. Shareholders may also be able to apply the principles to other listed companies and legal persons.

## *Eumedion principles*

### *Process and accountability*

1. The supervisory board<sup>24</sup> is responsible for the drafting of a remuneration policy for the management board, as well as for the implementation and the results of this policy.
2. The remuneration policy for the management board and amendments to this are adopted by the general meeting. Schemes in the form of shares or rights to subscribe for shares and amendments to such schemes are submitted separately to the general meeting for its approval.
3. The supervisory board renders account in the remuneration report for the implementation and the results of the remuneration policy for the management board. The remuneration report shows how the actual payments, a.o. any variable elements of the remuneration, derive from the remuneration policy adopted, so as to enable the general meeting to monitor the implementation of this policy. The remuneration report also contains, if applicable, a meaningful explanation of the use of 'discretion' by the supervisory board under the remuneration policy as adopted by the general meeting of shareholders
4. Companies are recommended to put the remuneration report to a vote as a separate item on the agenda at the general meeting. If the supervisory board does not put the remuneration report to a vote at the general meeting, shareholders are unable to express their opinion directly on the implementation of the remuneration policy by the supervisory board. In that event, shareholders may take the remuneration report into consideration when deciding on their voting behaviour for other items on the agenda.
5. The supervisory board assesses annually, partly on the basis of the results, whether the remuneration policy for the management board is still appropriate for the company. The remuneration policy for the management board is comprehensively evaluated at least once every four years and the general meeting adopts continuation of the existing policy or modifications to this policy.

### *Structure and content*

6. The remuneration policy for the management board is aligned with the long-term strategy of the company and the corresponding goals. The remuneration policy for the management board contains no stimuli that may be detrimental to the task entrusted to the management board of serving the long-term interests of the company.

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<sup>24</sup> In the event that the company has decided to include executive directors and supervisory directors in a single company body (a one-tier management structure), the principles set out in this document that apply to "the supervisory board" also apply to the supervisory or non-executive directors. Wherever this document refers to "the management board" or "members of the management board" it should also be understood to refer to executive directors in the case of companies with a one-tier management structure.

7. The structure and the amount of the remuneration of management board members are in keeping with the company's general remuneration policy. The supervisory board realizes that management board members are required to serve as examples to the other employees of the company.
8. The remuneration of management board members is based on a fixed salary. Any variable elements of the remuneration are subject to a maximum determined in advance. The (conditional) granting and payment of variable elements of remuneration depend on the achievement of goals<sup>25</sup> established in advance and also on the manner in which these goals have been achieved<sup>26</sup>.
9. The term for the unconditional granting of long-term variable remuneration elements is long enough to do justice to the long-term strategy of the company and the corresponding goals. This term is generally at least three years.
10. Companies are recommended to also base the granting of variable remuneration elements on environmental, social and/or governance goals. These goals are clear, quantified, time-bounded and stretching, have a direct relation with the company's strategy and the operational. The goals are measurable and transparent and linked to the company's performance.
11. The supervisory board has discretionary powers<sup>27</sup> relating to the unconditional granting of long-term variable remuneration elements in order to counteract unfair consequences, such as in the event of a takeover and/or dismissal.
12. The rules relating to variable elements of remuneration contain a provision that variable remuneration elements that have already been made unconditional and/or have been paid can be recovered if it becomes clear in due course that they have been wrongly granted (in part), on the basis of incorrect (financial) information. In this event, the supervisory board initiates a procedure to recover the remuneration elements in question.

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<sup>25</sup> The term "goals" does not only include financial goals.

<sup>26</sup> The risks taken are among the factors that can be borne in mind in this context.

<sup>27</sup> The term "discretionary powers" looks primarily on the ability of the supervisory board to make downward adjustments to the size of the variable, unvested, remuneration components. Upward revision cannot be excluded, but may only be used if the pay-out of variable remuneration components would be that low that it may conflict with the standards of reasonableness and fairness.

## **Appendix II: Eumedion recommendations on the delegation of power to issue shares**

### **a) Governing bodies involved in delegation.**

In view of the statutory division of tasks and powers within the company, it is most obvious that where the power to issue shares is delegated, the board of directors is instructed to issue them by the annual general meeting. For the same reason, the articles of association or the resolution to delegate must state that the issuing of shares based on this delegation requires the prior approval of the supervisory board.

The resolution to delegate may lay down the circumstances in which a share issue based on this delegation does not require the prior approval of the supervisory board, e.g. shares issued as part of a staff participation scheme approved by the general meeting.

There is no reason to subject the general meeting's delegation of its statutory powers to the approval of another body within the company, such as the supervisory board.

### **b) Agenda items and explanatory note**

A note on the proposal to delegate the power to issue shares must be published explaining the reasons for this proposal and the conditions under which the power to be delegated is to be exercised (including the maximum number of shares to be issued, the delegation period and the method of determining the issue price). This explanatory note must be placed on the company's website and lodged at the company's office for perusal.

Where the power to issue different types of shares is delegated, these proposals must be separate agenda items with separate explanatory notes. Where the power to issue shares is delegated with different objectives in mind (e.g. proposed acquisitions or staff participation schemes), these objectives must be itemised in the explanatory note, and delegation of the power to issue shares of the same class but with different objectives must be separate agenda items.

### **c) Maximum number of shares to be issued**

The maximum number of ordinary shares or financing preference shares to be issued on the basis of the resolution to delegate must be geared to the company's reasonably expected financing requirements (e.g. on account of acquisitions or reorganisations) during the period for which delegation is being requested. The reasons for this maximum number must be given in the notes to the proposal.

If no material financing requirement is envisaged in the proposed delegation period, an authorisation to issue ordinary shares or financing preference shares that may be used for any purpose may relate to not more than 10% of the subscribed capital after issue (including issuance relating to stock dividend and/or employee (stock) option plans). An authorisation to issue ordinary

shares or preference shares that may be used for mergers and acquisitions during that delegation period may also relate to not more than 10% of the subscribed capital after issue.

**d) Delegation period**

The power to issue shares may be delegated for a period not exceeding 18 months from the time of the resolution to delegate.

The resolution to delegate must state whether the delegation can be withdrawn by the annual general meeting.

Where a delegation period is still in progress, the proposal must be worded as an extension of this current delegation, to prevent a lack of clarity as to whether the current delegation will continue alongside the delegation to be granted.

**e) Permitted issue price**

It is within the power and the responsibility of the board of directors as the governing body to which the power to issue shares has been delegated and of the supervisory board as the supervisory body to determine an issue price which will take into account the interests of all concerned, including the interests of the shareholders in particular.

If the issue price is materially, i.e. more than 10%, lower than the average market price of the share concerned over the previous three-month period, the board of directors must state this by way of a press release and on the company's website in an explanatory note concerning this issue price.

The shareholders' interest in preventing dilution as a result of the issue price being too low is protected by their statutory preferential right, in respect of which please refer to the recommendation at (f).

**f) Precluding and restricting preferential rights**

A share issue in return for a contribution lower than the market price at the time of issue disadvantages the holders of shares already issued as an issue in return for a lower contribution will reduce the value of their shares. The statutory pre-emption right or the negotiable claim which they receive in this connection protects them against this or compensates for the reduction in value respectively. This safeguard is lost if both the power to issue shares and the power to preclude or restrict the preferential right are delegated to the board of directors.

Such a combined resolution to delegate must therefore provide that:

- (i) when these powers are jointly exercised by the board of directors, the value of the contribution must not be more than 10% lower than the average market price over the three-month period prior to the share issue; and

- (ii) a board decision based on this delegation is placed on the company's website, together with an explanation and notes on the proposed contribution.

In addition, the articles of association or the resolution to delegate must state that any board decision based on this delegation requires the prior approval of the supervisory board.

#### **g) Anti-takeover preference shares**

Anti-takeover preference shares are only taken:

- (i) as a temporary, necessary and proportionate protection against a specific threat to the continuity of the company or its policy, or a specific threat to the interests of the company, its business, the shareholders, the employees and other stakeholders and its business and after careful consideration of these interests;
- (ii) by a legal entity of which the board of directors is independent<sup>28</sup> from the company;
- (iii) up to a maximum which may not exceed 100% of the nominal amount of the previously subscribed shares<sup>29</sup>; and
- (iv) with as objective to enable the board of directors and the supervisory board of the company to enter into a constructive dialogue with the bidder, to explore possible alternatives, to inform the shareholders of the company or to protect the continuity of the company or its policy and the interests described under (i). Within six months after the issuance of anti-takeover preference shares, the board will issue a statement of the results or of 'the state of play' and will organize an extraordinary general meeting to discuss this statement with the shareholders.

In the event of a proposal to delegate the power to issue anti-takeover preference shares which will be exercised by granting a call option, the explanatory note must contain a description of:

- (v) the (draft) option agreement containing the conditions under which the option can be exercised;
- (vi) the maximum number of protective preference shares that can be issued;
- (vii) the maximum period for which the protective preference shares can be held;
- (viii) the conditions under which the company can withdraw the anti-takeover preference shares; and
- (ix) the composition of the board of directors of the legal entity with which the option agreement has been or will be concluded.

Where a call option has been issued in respect of anti-takeover preference shares, the company will provide the information referred to above (at (v)-(ix)) each year in its annual report and will the

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<sup>28</sup> I.e. independent from each other, the company board and any partial interest.

<sup>29</sup> Assuming that the authorised capital has been divided into shares of the same value as specified in section 2:118, par. 2 Civil Code.

general meeting of shareholders not ask for an authorisation of the management board to issue anti-takeover preference shares by themselves.

## **Appendix III: Eumedion recommendations on the authorization to repurchase own shares and on accountability for the dividend policy**

### **1. Recommendations on delegation of the power to repurchase own shares**

(a) **Organs involved in delegation.** In the event of the delegation of the power to repurchase own shares, the management board is designated by the general meeting for this purpose. If shares are actually repurchased on the basis of the granted authorization to repurchase, the repurchase requires the prior approval of the supervisory board. In the case of a one tier board structure, the actual repurchase requires the approval of the non-executive board members.

(b) **Placement on the agenda and explanatory notes.** A clear explanatory note must be provided on the item on the agenda concerning delegation of the repurchasing powers. This note must set out the reasons for the proposal and the conditions for the exercise of the powers to be delegated (including the maximum number of shares to be repurchased, the delegation period and the method of establishing the repurchase price). In the event of delegation of the powers to repurchase different kinds of shares, these proposals must be included as separate items on the agenda with separate explanatory notes.

(c) **Maximum number of shares to be purchased.** The company is permitted to *acquire* shares to an amount of no more than half of the issued capital during the delegation period. If no material reorganization of the capital structure is foreseen in the delegation period envisaged, however, the company is entitled, in principle, to *hold* no more than 10% of the issued capital in own shares at any time during this delegation period. This means that the maximum number of own shares that a company has “on the shelf” at any moment must not, in principle, exceed 10% of the issued capital. If a material reorganization of the capital structure is foreseen during the delegation period envisaged, the number of own shares that may be held at any time during the delegation period may be raised to 20% of the issued capital<sup>30</sup>. The company must, however, provide a clear explanation for authorization of this kind. If the company wishes to repurchase more of its own shares within the authorization period, the own shares previously repurchased must first be withdrawn, which requires a resolution by the general meeting. It is advisable, therefore, certainly in the event of a material reorganization of the capital structure, that the request for authorization to repurchase own shares should be accompanied by a request for authorization to withdraw the shares repurchased.

(d) **Re-issue of repurchased shares.** When authorization for the repurchase of own shares is requested, it must always be clearly stated whether it is intended to re-issue these shares (in

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<sup>30</sup> Other maximums may apply in the event of a proposal to purchase financing preference shares and/or protective preference shares.

connection with stock option and/or share plans for example). In the absence of an explanation of this kind, it must be assumed that the shares repurchased will not be re-issued. Repurchased shares may not be issued to a party with the objective of facilitating a takeover, or of preventing a takeover by another party ('targeted stock placement').

(e) **Delegation period.** Delegation of the power to repurchase own shares can be granted for a maximum period of 18 months as from the moment of the resolution to delegate. The resolution to delegate must state that the general meeting is entitled to withdraw the delegation and the conditions for withdrawal must be set out in detail in the resolution to delegate. It is preferable in the event that a delegation period is still current, to formulate the proposal as an extension to this current delegation, in order to prevent uncertainty as to whether the current delegation will continue to exist alongside the new delegation.

(f) **Method of repurchase.** When authorization for the repurchase of own shares is requested, it must be clearly stated how the shares in question will be repurchased; on the stock exchange or by a different method. It must always be clear that all shareholders in equal measure can offer their shares to be repurchased. In unusual cases in which shares from one or a number of shareholders are repurchased, clear reasons must be provided for these transactions and these must be clearly apparent to all shareholders.

(g) **Permitted repurchase price.** The repurchase price must not be higher than 110% of the market price of the share; the market price being the average of the highest price on each of the five days of trading prior to the date of acquisition. If the management board requests authorization for a higher repurchase price, a clear explanation must be provided for this.

(h) **Rate of repurchase.** Repurchase transactions are not intended to influence the price of the share temporarily and the company must provide clear information, therefore, on what precautions have been taken to prevent repurchase transactions from influencing the price on the stock exchange each day. The maximum number of shares to be repurchased per day of trading must always be stated (or what maximum percentage of the shares traded each day), how repurchase transactions are connected with the share-price related objectives in the remuneration policy and which internal or external party has been charged with the repurchase.

(i) **Transparency on repurchase transactions.** The company will include a summary of transactions in the financial statements showing developments in the number of own shares repurchased, in order to provide clear insight into the development of the repurchasing transactions during the financial year.

## **2. Recommendations dividend policy**

- (a) **Reporting.** The dividend policy must be clearly and transparently described at a place in the annual report. Transparency would benefit if the relationship between the dividend policy and other possible relevant aspects of the strategic policy of the company could be clarified; these aspects could relate to long-term development, innovation, mergers and takeovers, and executive remuneration. A company that is paying dividend states which criterion or criteria is/are applied in determining the rate of the dividend and provides sound substantiation for this. A company that is not paying dividend (as yet) reports in the annual report why it is not doing so (as yet) and when and under what conditions the management board will actually consider paying dividend. A company that is considering paying dividend states when it is possible that dividend may be distributed.
- (b) **Placement on the agenda.** A company's dividend policy is dealt with and accounted for as a separate item on the agenda for the general meeting.

#### **Appendix IV: Eumedion guidance for the explanatory notes to the nomination for (re)appointment of the statutory auditor**

The following is stated in Best Practice Provision V.2.3 of the Dutch corporate governance code: "At least once every four years, the management board and the audit committee shall conduct a thorough assessment of the functioning of the external auditor within the various entities and in the different capacities in which the external auditor acts. The main conclusions of this assessment shall be communicated to the general meeting for the purposes of assessing the nomination for the appointment of the external auditor." Eumedion assumes that, in line with current views on good corporate governance, the audit committee will take the lead in making the assessment, using the input from the management board and the internal auditor.

Within the context of the "thorough assessment of the functioning of the external auditor" referred to in the Code, Eumedion participants would welcome the provision of the following information in the explanatory notes to the nomination for the (re)appointment of the statutory auditor:

- a) A description of the process of arriving at this thorough assessment of the functioning of the statutory auditor.
- b) A statement of the main conclusions of the thorough assessment, addressing also the following subjects: i) the quality of the audit; ii) the adequacy and interpretation of the audit assignment; iii) the quality of the content of the reports to the management board and to the audit committee; iv) the independence of the statutory auditor; v) the general conduct of the statutory auditor, including his professional scepticism; vi) the expertise and membership of the audit team; vii) the costs; and viii) the application of the Dutch Audit Firm Governance Code by the audit firm in question.

The supervisory board may decide in response to the thorough assessment to initiate a procedure of inviting tenders for the audit assignment. Eumedion considers it advisable that this be done at least once in seven years. The tendering procedure is announced in the report of the supervisory board one year before this procedure is implemented. In the event that a tendering procedure is decided on, Eumedion participants would welcome the provision of the following information on the tendering procedure in the explanatory notes to the proposal for the appointment of a new audit firm or for reappointment of the present audit firm:

- a) The number of audit firms approached to submit a tender.
- b) A description of the selection criteria, which is consistent with the company's policy regarding the independence of the statutory auditor and the quality controls at the audit firm in question.
- c) A description of the selection process.
- d) The decisive reason(s) for the recommendation of the audit firm in question.
- e) The scope of the audit assignment.

- f) The policy on any consultancy assignments to be carried out by the same audit firm (approval procedure, application of a maximum percentage of the total auditing costs, etc.).
- g) The proposed term of appointment of the statutory auditor;
- h) In the case of a proposal for reappointment, the aggregate tenure of the incumbent audit firm.

## Appendix V: Eumedion Best Practices for Engaged Share-Ownership

### 1.0 Preamble

1.1 Eumedion participants believe that responsible use of the rights attached to shares strengthens the checks and balances within listed companies, which is key to creating long term value for the company and all its stakeholders, including shareholders. Responsible behaviour not only means that Eumedion participants cast ‘informed’<sup>31</sup> votes at shareholder meetings, but also includes the monitoring of investee companies’ activities. Maintaining an ongoing dialogue with company boards may also fall under monitoring. Included in this monitoring as well are important aspects relating to corporate governance, including environmental and social (ES) aspects in the field of risk management, disclosure and remuneration policy, supporting the company in respect of good governance and consulting other shareholders and stakeholders where appropriate. Furthermore, responsible behaviour requires high standards of transparency, probity and care on the part of institutional investors themselves. Eumedion has drafted this series of best practices as guidance for its participants – which include pension funds and the asset managers of these pension funds – in fulfilling their essential role in the governance of listed companies.

1.2 The minimum standards for Eumedion participants are set out in the applicable legislation and regulations and in the Dutch corporate governance code. Section IV.4 of the Dutch corporate governance code contains two principles and six best practice provisions for institutional investors. Dutch pension funds, life insurers and investment firms have a statutory obligation to report on their compliance with these principles and best practice provisions, in accordance with the “apply or explain” rule. The statement on the degree of compliance must be shown in the annual report or placed on the website of the institutional investor. The best practices set out below apply to Eumedion participants in addition to the Dutch corporate governance code to promote responsible and engaged share-ownership.

1.3 Many institutional investors have an international share portfolio and shareholder rights and corporate governance models differ from country to country. The transparent use of these best practices means that ultimate beneficiaries and clients, as well as the Dutch listed companies will be able to discern the lines along which Dutch and non-Dutch Eumedion participants interpret their current shareholder rights. Furthermore, these best practices aim to improve the understanding and communication between Dutch listed companies and Eumedion participants. The best practices are not binding in the way that Dutch legislation and the Eumedion articles of association are binding, but they are not free of obligation either. Eumedion participants endeavour to implement the best practice

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<sup>31</sup> An 'informed' vote means that the voting right is exercised in accordance with the participant's own voting policy and, in the event that the participant makes use of voting advice from third parties, that it forms its own opinion on the voting recommendations made by this adviser.

provisions as well as possible. It is also expected of the Eumedion participants that they observe the "apply or explain" rule, just as they do with the Dutch corporate governance code. In reporting terms, this entails providing a statement on the institutional investor's website or in its annual report containing:

- a description of how the best practices have been applied;
- disclosure of the information listed under best practices 2, 5, 6 and 8; or
- an explanation, if these elements have not been applied.

Most of the best practices set out below are accompanied by guidance. This guidance provides a further explanation of the best practice in question, sometimes by giving examples, but contains no additional norms.

1.4 The best practices are closely in keeping with Eumedion's objective, but they do not only serve an internal goal. By applying the best practices, Eumedion participants also demonstrate that they are conscious of the greater responsibility that society expects of both Dutch and non-Dutch institutional investors, because they hold the majority of the shares in the largest Dutch listed companies and manage other people's money. The best practices are also in line to the greatest possible extent with international guidelines on the behaviour required of institutional investors, such as the *UK Stewardship Code*, the *Statement of Principles on Institutional Shareholder Responsibilities* from the International Corporate Governance Network (ICGN), the *United Nations Principles for Responsible Investment* (UNPRI) and the *Code for External Governance* of the European Fund and Asset Management Association (EFAMA). A large degree of similarity between these different sets of best practices is also desirable, because more than 70% of the shares in the largest Dutch listed companies are held by non-Dutch parties and conversely, many Dutch Eumedion participants also hold shares in non-Dutch listed companies.

1.5 Eumedion acknowledges that some participants do not have the human resources to become directly involved in a dialogue and other engagement activities. This could also be the case when the invested capital is (largely) managed by an external asset manager. Eumedion would like to urge these participants to mandate their asset managers to do dialogue and other engagement activities on their behalf as the occasion arises and to carefully scrutinize the reports from these managers with regard to the dialogue and other engagement activities. In addition, Eumedion also acknowledges that asset managers must act in accordance with the wishes of their clients. External asset managers who are Eumedion participants are expected, however, to urge their institutional clients who are not Eumedion participants to apply the best practices set out below, or to mandate their external asset managers to apply the best practices on their behalf. A number of participants invest solely in (institutional) investment funds and not directly, therefore, in shares in Dutch listed companies, which means that these participants are themselves unable to exercise the voting rights on these shares. The participants

concerned will be considered to be in compliance with the best practices when the manager of the (institutional) investment funds applies the best practices or other (international) codes or guidelines with similar objectives, and the same applies to participants who have their invested capital managed by a specific pension fund manager. There are also participants that have issued so-called passive mandates to asset managers. These participants are expected to have taken the policies on dialogue, engagement and voting pursued by the asset manager in question into consideration when choosing that asset manager.

1.6 Some Eumedion participants have to apply the *UK Stewardship Code* or follow other national or international standards that have similar objectives to the best practices set out below. These participants should not feel that application of the best practices set out below doubles or confuses their responsibilities. Disclosures made in respect of other (inter)national standards can demonstrate the extent to which participants have implemented the best practices set out below. It may be justified to follow an alternative guideline in specific cases and under particular circumstances, if the same behaviour can be achieved by applying other standards or a participant's own standards of the same nature.

1.7 Eumedion participants are encouraged to enter into a dialogue with Dutch listed companies and to do so collectively where appropriate. When entering into dialogue with companies, institutional investors obviously respect the relevant statutory rules and guidelines from regulatory authorities, such as those intended to prevent the use of insider information<sup>32</sup>. Some best practices are intended to stimulate cooperation and consultation between institutional investors. Such forms of consultation are generally not based on an agreement to pursue a *sustained* joint voting policy and therefore do not qualify as 'acting in concert'. As regards *acting in concert* in relation to the submission of a (collective) notification of a substantial holding when cooperating with other investors, the Netherlands Authority for the Financial Markets (AFM) has issued some guidelines. Institutional investors are encouraged to take note of these guidelines<sup>33</sup>.

1.8 Although the best practices are addressed to Eumedion participants alone, institutional investors that are not Eumedion participants yet, including non-Dutch institutional investors, are encouraged to consider participation in the near future and to commit to the best practices. This can help in building a critical mass of institutional investors committed to transparency and a high quality dialogue with Dutch listed companies. This contributes to helping improve the governance and performance of companies and, consequently, the long-term returns for shareholders and other stakeholders.

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<sup>32</sup> See Chapter 5.4 of the Financial Supervision Act [Netherlands]: <http://english.minfin.nl/dsresource?objectid=76287&type=org>. See also the guidance regarding one-on-ones: <http://www.afm.nl/nl/professionals/diensten/veelgestelde-vragen/marktmisbruik/one-on-ones.aspx?perpage=10>

<sup>33</sup> See: [http://financieelblijsluiter.com/layouts/afm/default.aspx~/media/files/brochures/2009/acting\\_in\\_concert\\_eng.ashx](http://financieelblijsluiter.com/layouts/afm/default.aspx~/media/files/brochures/2009/acting_in_concert_eng.ashx)

1.9 The best practices facilitate a high standard of engaged share-ownership. They comprise general guidelines on policy, structure and processes, thus providing Eumedion participants with the scope to anticipate the widely diverging situations in which the best practices will be applied. Eumedion participants, therefore, have the scope within the framework of the best practices to decide for themselves how they should act. The Eumedion secretariat will annually monitor the compliance of Eumedion participants with the best practices on the basis of information including the published reports on the application of the best practices referred to in paragraph 1.3. The results will be reported to the General Board of Eumedion and Eumedion participants will receive a progress report every year, which will also contain examples of best practices. A summary of the progress report will be made public.

## **Best Practices**

### **Best practice 1**

Eumedion participants monitor their Dutch investee companies.

#### *Guidance*

The monitoring of the investee companies is important when entering into any dialogue with a company, or developing other engagement activities. Monitoring is also important in relation to holding or selling the shares in the company in question.

The monitoring process is considered to comprise, but not exclusively, careful scrutiny of the environmental and social policies and the governance structure of the company by Eumedion participants. In this context, Eumedion participants make a thorough assessment of the reasons provided by the company for any non-compliance with the best practice provisions of the Dutch corporate governance code.

### **Best practice 2**

Eumedion participants have clear policies with regard to the exercise of their shareholders' rights, which may include entering into dialogue with Dutch investee companies and other engagement activities. They report at least once per year on the implementation of their policies.

### **Best practice 3**

Eumedion participants have clear policies for dealing with situations in which it does not prove possible to convince the board of the Dutch investee company of their stances and differences of opinion between the board of the investee company in question and the shareholders remain unsolved.

### *Guidance*

Elements for a policy of this kind may include:

- Writing a letter to the management and/or supervisory board in which the matters of concern are explained;
- Holding additional meetings with the management and/or supervisory board, specifically to discuss matters of concern;
- Holding meetings with other stakeholders, such as other shareholders, banks, creditors, the works council and non-governmental organisations (NGOs);
- Expressing concerns in a shareholders' meeting;
- Issuing a public statement;
- Intervening jointly with other institutional investors on specific issues;
- Requesting that certain subjects be placed on the agenda for the shareholders' meeting or asking that an extraordinary shareholders' meeting be convened;
- Submitting one or more nominations for the appointment of a member of the management board and/or supervisory director as appropriate;
- Taking legal action, when appropriate, such as initiating inquiry proceedings at the Enterprise Chamber of the Amsterdam Court of Appeal;
- Selling the shares.

### **Best practice 4**

Eumedion participants are willing to deal collectively with other Eumedion participants and other investors where appropriate.

### **Best practice 5**

Institutional investors may have other business relations with Dutch investee companies apart from the shareholder relationship alone. Eumedion participants take steps to mitigate conflicts of interest arising from these different roles. Eumedion participants have clear and robust procedures in place for the action to be taken in the event that divergent or conflicting interests arise. The procedures are publicly disclosed. Material conflicts of interest will be disclosed to the institutional clients affected.

### *Guidance*

It is advisable in certain situations for clients to be aware of the possible existence of other interests involving the institutional investor and the company, apart from the shareholder's interest alone. This can occur, for example, in the situation in which the investor in question also offers financial products (such as insurance contracts) to the enterprise, or when a member of the management board or the supervisory board of the institutional investor is also a member of the management board or

supervisory board of the company in question. It is also possible for an institutional investor that invests for a pension fund to hold shares in a company that sponsors the pension fund concerned, or for an institutional investor to be affiliated in some way with a company for whose shares a public bid has been launched.

When participating in collective dialogue or other engagement, participants would be wise to take their policies on conflicts of interest and insider information into account in advance of the dialogue.

### **Best practice 6**

Eumedion participants have a clear policy on voting and publicly disclose this policy. Eumedion participants report at least once per year on the implementation of their voting policy<sup>34</sup>.

### **Best practice 7**

Eumedion participants cast informed votes<sup>35</sup> on all the shares they hold in Dutch companies at the general meeting of these investee companies. In the event that the Eumedion participant casts a withhold or against vote on a management proposal, the Eumedion participant will explain the reasons for this voting behaviour to the company management, either voluntarily or on the request of the company in question.

#### *Guidance*

The Dutch corporate governance code states that institutional investors should publish their voting policies, the implementation of these policies (on an annual basis) and how they have voted (on a quarterly basis). Best practice 7 requests Eumedion participants to use their voting rights in a well considered manner and in line with their voting policies.

Eumedion participants who participate in an asset pool or in an (institutional) investment fund ensure that they feel able to endorse the voting policy of the manager of the asset pool or of the investment fund, that they monitor the actual voting behaviour of this manager and can withdraw from the pool or the fund, where feasible, if they do not agree with the voting policy and/or its implementation.

### **Best practice 8**

Eumedion participants publicly disclose at least once in a quarter how they voted the shares in Dutch investee companies<sup>36</sup>.

#### *Guidance*

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<sup>34</sup> This best practice corresponds with best practice provisions IV.4.1 and IV.4.2 of the Dutch corporate governance code.

<sup>35</sup> See footnote 31 for a definition of "informed votes".

<sup>36</sup> This best practice corresponds with best practice provision IV.4.3 of the Dutch corporate governance code.

Preferably at individual company level, Eumedion participants publish for each item on the agenda whether they voted in favour of or against, or abstained.

**Best practice 9**

Eumedion participants take aspects relating to environmental and social policy and to governance into account in their policies on the exercise of their shareholder rights, which may include entering into dialogue with listed companies and other engagement activities.

**Best practice 10**

Eumedion participants do not borrow shares solely for the purpose of exercising voting rights on these shares. They consider recalling their lent shares before the voting registration date for the relevant general meeting of the relevant Dutch investee company, if the agenda for this general meeting contains one or more controversial subjects.

*Guidance*

The above best practice is included in the policy on securities lending around the voting record date for the general meeting.

In the event that an institutional investor is engaged in a dialogue with the investee company on certain issues, outside the context of a shareholders' meeting, it is advisable that the institutional investor's position (the extent of its legal and economic interest) is made completely clear to the company on its request.

## Appendix VI: ICGN Securities Lending Code of Best Practice

The lending of securities and especially of common shares is an increasingly important practice which improves market liquidity, reduces the risk of failed trades, and adds significantly to the incremental return of investors. However, we have found that there is widespread misunderstanding of securities lending transactions on the part of those not directly involved in the process. The word 'lending' has itself misled many as in law the transaction is in fact an absolute transfer of title against an undertaking to return equivalent securities. Misconceptions as to its nature have led to loss of shareholder votes in important situations, as well as to cases of shares being voted by parties who have no equity capital at risk in the issuing company, and thus, no long-term interest in the company's welfare. Lenders' corporate governance policies may also be undermined through lack of coordination with lending activity. It is also imperative that there be as little risk as possible that a poll of the shareholders may be compromised through misuse of the borrowing process. To address these concerns the ICGN proposes this Code of Best Practice to its members. It encourages other concerned investors, market intermediaries, and public companies to take account of the Code where appropriate.

Three broad principles which apply to all areas of investment practice are here used to clarify the responsibilities of all parties engaged in stock lending. With their relevant applications in this area, they are:

First, **transparency**: the lending process, frequently handled today as a purely mechanical adjustment to custodial arrangements, should become subject to the same visibility and safeguards as any other transaction conducted on an owner's or beneficiary's behalf in a securities account.

Second, **consistency**: it is unreasonable to expect that lending agents can make subtle judgements as to when they should sacrifice some income in order to protect the lender's long-term economic interests and stewardship commitments. A clear set of policies which indicates with as little ambiguity as possible when shares shall be lent and when they shall be withheld from lending or recalled is necessary in order to ensure that similar situations are handled in the same way. Clear mechanisms should be set up to handle borderline situations. Neither the long-term economic interest in better governance nor the interest in maximising short-term remuneration should be allowed to exceed the parameters set for each by the stated policy of the primary lender\*.

Third, **responsibility**: responsible shareholders have a duty to see that the votes associated with their shareholdings are not cast in a manner contrary to their stated policies and economic interests. While fiduciaries have a duty to maximise economic returns to their beneficiaries, they equally have a fiduciary duty to protect their long-term interests through voting and other actions sometimes precluding lending. Fiduciaries also have a duty to ensure that the pursuit of more income is not subjecting their beneficiaries to greater risks. These responsibilities must be appropriately balanced according to the

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\* The asterik indicates when a term defined in Appendix III is used in the text for the first time.

primary lender's voting policy, in accordance with its ultimate beneficiaries' preferences. This responsibility lies with the primary lender, and not with its agents.

By properly following these broad principles best practice with regard to share lending can be achieved. The difficulty lies in applying them thoroughly. Staffers or agents responsible for voting and investment decisions should always have full transparency whether and what percentage of shares have been lent. Beneficiaries should always know which percentage their manager has voted of its position in a given portfolio company. Consistency may be lost when a lender with a policy to recall shares to vote "on important issues" cannot know in a particular country with an early record date what the issues to be voted upon will be. (This is the case in the United States and Canada.) Responsibility has been ignored when lenders, drawn by suddenly rising demand, lend shares under circumstances in which it is highly probable that they are being borrowed in order to alter the result at a shareholders' meeting, possibly to their own detriment.

Specific aspects of best practice follow from these broad principles. While simple to state, their application may be complex and involve many unsuspected technical adjustments. We have therefore sought to provide more detailed guidance and explanation in the attached appendices. The basic tenets of best practice, however, are:

- 1. All share lending activity should be based upon the realisation that lending inherently entails transfer of title from the lender to the borrower for the duration of the loan.** Most economic rights of the lender can be preserved through contractual agreements with the borrower. Those involving the issuer, however, such as the right to vote, or one's continuity on the share register, **cannot** be preserved in this way. If an investor wishes to vote its lent shares or protect its legal interests as a registered shareholder, it **must** recall the shares.
- 2. During the period of a stock loan, lenders may protect their rights only with the borrower, since they have no rights with the issuer of the shares which have been lent.** Stock loans are normally collateralised at more than 100% of the current market value of the loan. The collateral may be cash, high-quality debt securities, or equivalent equity securities. Lenders must ensure that this collateral, together with any contractual claims upon the borrower, adequately protects their interests for the duration of the loan.
- 3. Institutional shareholders should have a clear policy with respect to lending, especially insofar as it involves voting.** A lending policy should clearly state, *inter alia*, the lender's policy with regard to recall of lent shares for the purpose of voting them. All lending conducted by the institution or on its behalf should be done in accordance with this stated policy.

**4. Lending policy should be mandated by the ultimate beneficial owners of an institution's shares,** whether they be another institution or corporate body or an assemblage of individuals.

**5. Where lending activity may alter the risk characteristics of a portfolio, the policy should state the extent to which this is permitted.** This involves the extent of lending activity, the quality of the borrowers, the quality of the collateral accepted for loans, and its nature: cash, other securities, or a combination of the two, as well as any questions as to changes in the duration of the portfolio, as well as its other risk characteristics.

**6. The returns from lending should be disclosed separately from other investment returns when reporting to clients or beneficiaries. They should not be hidden under management and other costs.** As lending has become an important source of revenue, it behoves institutions to disclose its extent to their clients or beneficiaries, as well as the extent to which investment returns and cost ratios are being driven by or ameliorated by the returns from lending.

**7. It is bad practice to borrow shares for the purpose of voting. Lenders and their agents, therefore, should make best endeavours to discourage such practice.** Borrowers have every right to sell the shares they have acquired. Equally the subsequent purchaser has every right to exercise the vote. However, the exercise of a vote by a borrower who has, by private contract, only a temporary interest in the shares, can distort the result of general meetings, bring the governance process into disrepute and ultimately undermine confidence in the market.

The ICGN affirms the principle that companies should know who controls the votes at their general meetings, and that this transparency should benefit all market participants. Considering the availability of market instruments that separate economic ownership from control, the ICGN believes that it has become desirable for companies and the broader market to be able to track significant divergence of voting power from declared economic ownership. The ICGN therefore invites the relevant market authorities to consider amending their holdings disclosure regimes to include the transfer of actual or contingent voting rights executed through the use of securities lending and derivatives.

The attached appendices attempt to delineate in full the responsibilities of the different parties, the sorts of circumstances under which the above principles might be compromised, and how these situations should be handled in accordance with best practice. They are intended as guidance. Best practice may be achieved by other mechanisms as long as the principles are kept in mind in devising appropriate procedures.

## **Appendix I to ICGN Securities Lending Code of Best Practice: Duties of the Respective Parties to a Lending Transaction**

### **A. Lender's Responsibilities**

a) *Policy on Voting and Recall of Loaned Shares* – The fund, fund sponsor, or principal manager\* of a portfolio or fund from which shares are loaned (hereafter the primary lender\*) should be responsible for drafting and publishing a general policy that clearly sets forth the scope of lending activity, and under what circumstances, if any, this activity is to be subordinated to voting and to the lender's duties as a long-term shareholder.

b) *Terms of Master Agreement* – A Master Lending Agreement among the primary lender, the borrower,\* and any custodians, agents or other parties involved in the loan transaction should implement these policies, the attendant procedures, including the procedures for recalling\* shares and whatever penalties there are for non-compliance, and indicate the likelihood that shares may be recalled for voting purposes. Needless to say, the Master Lending Agreement should protect the lender's and the borrower's economic interests to the greatest extent possible in the jurisdiction involved.

c) *Disclosure within the Lender's Ownership Chain\** – The primary lender's trustees or directors should effectively communicate their policies and procedures to designated executives at the lending institution and at any agent organisations involved in the investment, lending, or voting of those shares, as well as with those responsible for corporate governance for the portfolio or fund in question. All changes in actual positions due to any lending activity should be updated daily to all those executives charged with investing or voting the shares.

d) *Responsibility for Compliance* – The primary lender should be responsible for ensuring that its policies and procedures are practicable, that they fulfil the principles expressed herein, and that they are properly administered no matter what the lender's structure and division of responsibilities among different business units or agent companies.

e) *Dispute Resolution* – The primary lender or its principal manager should establish and administer specific procedures to resolve disputes that may arise in connection with the implementation of its lending policy. A record should be kept of each of these disputed cases and the decision should be communicated to all the designated parties within the lender's organisation.

f) *External Disclosure* – The revenues from lending activity should be disclosed separately to the portfolio's or the fund's beneficiaries. If the jurisdiction is one in which voting must be disclosed to beneficiaries, lenders should also disclose when shares were not voted because they were out on loan.

g) *Lending Agents* – The obligations of any agent charged with conducting lending activity on behalf of a primary lender are normally set out in a contract. It is important that primary lenders ensure contracts are worded so as to incorporate the maintenance of best practice, including, where appropriate, the

terms and conditions of the Master Lending Agreement. Ultimate responsibility for maintaining best practice in lending policy is the duty of the primary lender.

### **B. Borrower's Responsibilities**

a) *Recall of Borrowed Shares* – Borrowers should agree to return equivalent shares to those borrowed promptly upon the lender's request whether these are in the borrower's possession or more likely must be purchased in the market. All properly executed requests for recall must be treated as equally valid.

b) *Non-Voting of Borrowed Shares* – It is never good practice for borrowers to exercise voting rights with respect to shares they have borrowed, except in the rare circumstances where they are acting pursuant to the lender's specific instructions. This limitation is not binding upon a subsequent *bona fide* purchaser of borrowed shares.

c) *Special Terms of Agreement* – Borrowers should comply with any additional terms agreed with the lender and should, to the extent possible, communicate these terms to other parties on whose behalf they are carrying out the borrowing.

d) *Accountability and Prevention of Abuses* – When borrowing shares for a third party client, borrowers should use their best efforts to ensure that the principals on whose behalf they are acting understand that they are supposed to comply with best practice, as set forth in this Code.

### **C. Recommended Actions for Issuers to Ameliorate the Effects of Lending**

a) *Timely Notice of Shareholder Meetings and Other Transactions* – Issuers should publish and distribute a Notice of Meeting, Agenda and other disclosure documents in sufficient time for lenders and borrowers of shares to comply with their policies and best practices as set forth in this document, including public notice of the issues well before any significantly advanced record date.

b) *Separation of Record Dates for Dividend Payments and Shareholder Meetings* – To minimise the effect of share lending for dividend swaps\* upon shareholder participation and share voting, issuers should not set dividend record dates less than 30 days in advance of a shareholder meeting or record date (whichever is relevant for voting) nor less than 15 days after the shareholder meeting (or record date).

c) *Tabulation* – Issuers have a duty of care in their record keeping and administration of shareholder voting to identify and expose abuses in the voting of borrowed shares and to prevent double voting of shares. If the custodians' practice of using commingled accounts interferes with that responsibility, issuers have a duty to call public attention to the problem, and to work with custodians to ameliorate it wherever practicable.

## **Appendix II to ICGN Securities Lending Code of Best Practice: Guidance on Best Practices Associated with the Responsibilities of Primary Lenders, Lending Agents, and Borrowers**

### *1. Voting and share lending.*

1.1. The voting right is normally inseparable from the share in which it inheres.

1.2. Accordingly, except in the rare case in which some private treaty provides for the separation of voting right from the share (and this is permitted by the issuer and by any applicable law), the primary lender of a share loses his voting right for that share. Until and unless a recall is executed, and an equivalent share is delivered to the lender, he is disenfranchised with respect to that share.

1.3. Any subsequent bona fide purchaser of that share, whether his ownership come as a result of purchase of a share sold short\* by the borrower, or of delivery in lieu of a failed settlement,\* acquires the voting right together with all the other indicia of ownership. As a matter of market practice, he will have no idea that his share had formerly been borrowed from someone else. As far as the issuer is concerned, the share has changed hands.

1.4. With respect to ownership rights, the initial borrower is in a different position than any subsequent owner to whom the shares are sold, as the initial borrower knows that the shares were borrowed, and that it retains rights over the collateral\* posted in lieu of payment.

### *2. Improper Lending Practices.*

2.1. The borrowing of shares for the primary purpose of exerting influence or gaining control of a company without sharing the risks of ownership is a violation of best practice. Similarly, the borrowing of shares in order to deliberately reduce or suppress the vote at a shareholders' meeting is bad practice.

2.2. Accordingly, the borrowing of shares for the purpose of exercising the right of the shareholder's vote is to be discouraged by all lenders.

2.3. The borrower of a share, for whatever purpose, should not vote that share without the express permission of the lender, and in accordance with his instructions.

2.4. Similarly, the holder of a share as collateral should not vote that share, unless specifically given the exclusive right to do so by private treaty with the borrower who provided the collateral.

2.5. The lender's Master Lending Agreement should specify that shares are not being lent for the principal purpose of voting those shares, and should provide clear guidance as to what circumstances might permit a borrower to vote borrowed shares as well as what the responsibilities of any lending agents might be in those circumstances.

2.6. No lender or lending agent should knowingly enter into a scheme in which he is making shares available to a borrower for the primary purpose of voting them, or of otherwise attempting to exert control upon the issuing company by means of the voting right attached to the borrowed shares.

*3. Lending policy, lending contracts, transparency, and disclosure.*

3.1. Policy on lending, and in what circumstances lending is to be considered subordinate to voting, should be a responsibility of the trustees or the directors of the fund or portfolio from which shares are to be lent.

3.1.1. A written statement of the lending policy should be communicated to any other entities up and down the chain of ownership which might have any reason to become involved with lending or voting decisions.

3.1.2. The lending policy statement should also be made available to the ultimate beneficiaries of the portfolio or fund. This document should make clear under what general circumstances loans are likely to be recalled for voting purposes, and the approximate extent of loan activity envisioned.

3.2. The lending contract should be negotiated with the full knowledge and active participation of the primary lender of the securities if the lending is to be done by an agent. Any subsequent changes to the contract or other departures from standard practice should be discussed beforehand with the primary lender or its manager responsible for the shares in question.

3.3. It is recommended that lenders rely upon a contract which protects their rights and provides full compensation or damages with respect to all corporate actions, as well as allowing for recall in the event of a vote the lender deems controversial and appropriate for recall.

3.4. In the event of failure to deliver like shares when they have been recalled for the purpose of voting, the penalties should be the same as for failure to deliver for any other reason.

*4. Communication of lending activity.*

4.1. It should be incumbent upon whoever is responsible for actual lending—whether it be a division of the primary manager, the primary manager’s custodian, or any other agent of the primary manager or the holding chain—to update the data on any lending activity and on attendant changes in the relevant portfolio. This data should be furnished to all those personnel responsible for management of that portfolio, and to those responsible for voting decisions and for the implementation of corporate governance policy.

4.2. Such data should be made available in a timely fashion, normally by the close of business each day.

4.3. If responsibility for portfolio management and/or voting decisions has been delegated by the primary manager to another agent not in the chain of control between the primary manager and the lending agent, a separate chain of communication should be set up, and the lending agent required to inform directly this entity (or these entities) of lending activity and changes in the composition of the portfolio resulting therefrom.

*5. Communication regarding proxy material, record or blocking dates, and decision dates.*

5.1. The following personnel are potentially in need of information regarding meeting agendas and dates, the text of proposals, key decision dates, and parameters for any proxy vote or other corporate action which might trigger a recall:

- (a) The portfolio manager directly responsible for buy and sell decisions concerning the stock in question
- (b) Whoever is responsible for proxy voting decisions regarding the same security
- (c) The party responsible for implementing corporate governance policy
- (d) The principal manager of the fund involved if different from above.

5.2. Primary lenders should ensure that the proper mechanisms for timely dissemination of this information are in place, so that all of these key decision makers are informed sufficiently ahead of decision deadlines that they may make appropriate judgments in accordance with their particular mandates. This may require some sort of routine distribution of communications from the custodian, and/or from other services.

*6. Resolution of disputes involving recall.*

6.1. The Primary Lender's Policy Statement, as well as the Master Lending Agreement, should prescribe a formal mechanism to resolve any dispute arising from a difference of opinion as to whether a given share should be left out on loan or recalled.

6.2. Such a dispute-resolving mechanism should fairly represent the different perspectives of investment managers, corporate governance staff, and the exigencies of lending.

6.3. Decisions should be made in accordance with the primary lender's stated lending policy, its governance policy, and the explicit objectives of the fund. The object is to resolve the conflict between short-term revenue maximization and longer-term investment or governance goals.

6.4. The decisions of the resolving mechanism should be a matter of record to be communicated to those responsible for setting and enforcing corporate governance policy at the primary lender or its manager.

## *7. Record dates.*

7.1. Record dates pose a special challenge to the lender of securities, as they may be significantly divorced in time from the date of the actual vote.

7.2. In those jurisdictions in which it has been the practice for the issuer to publish and distribute proxy material and the agenda of the shareholders' meeting only after the record date and only to shareholders of record on that date, it may be difficult or impossible for lenders to know whether they might want to recall shares for voting in advance of the record date.

7.2.1. To circumvent this conundrum, issuers should promulgate the agenda for upcoming shareholders' meetings publicly (e.g., by posting at the company's website) sufficiently in advance of the record date that lenders may have time to recall should they decide to do so. This is in keeping with the "Issuer's Recommended Actions" delineated in Appendix I. C. above.

7.2.2. In the absence of such provision by issuers, lending institutions in those jurisdictions can only make reasonable efforts to learn whether an upcoming shareholder vote is likely to be sufficiently controversial under their own voting guidelines that they should consider recalling the relevant share in advance of the record date.

7.2.3. Absent resources for such information gathering, it may be impossible for lenders to pursue a policy of recalling lent shares 'in the event of an important or controversial vote.'

7.3. When the record date or its functional equivalent is near in time to the shareholders' meeting, and the agenda has already been distributed some time before, this problem does not arise.

## *8. Dividend dates.*

8.1. Another common use of lending is for dividend swaps. For this strategy to be employed, the share must be lent over a dividend record date. Obviously, the lender loses the vote over that period, which may coincide with the meeting date, or the record date for voting in a record date jurisdiction.

8.2. Lending institutions should be aware of this hidden consequence of such a lending transaction.

8.3. Issuers are also urged to separate dividend record dates sufficiently from voting record dates or whatever other dates are ruling for eligibility to vote (e.g., reconciliation date, the date of the meeting, etc.), so that transactions of this type do not reduce the valid shareholder vote, or confuse the question of who is the proper beneficial owner entitled to vote.

## *9. Lending policy and risk.*

9.1. By lending shares, a portfolio's risk characteristics may be changed significantly. Normally, the standard contracts and practices in use successfully counter that possibility, but exceptions may exist.

9.2. In those markets in which the lender's margins are determined or affected by the reinvestment of the collateral required for the loan, additional assessments of risk are necessary, and additional controls

may be warranted to ensure that lending agents do not exceed the risk parameters appropriate for that portfolio.

*10. Disclosure of lending activity.*

10.1. As a general matter, lending activity is not reported to outside parties or to individual fund beneficiaries, except where provided for by contract or by law.

10.2. However, the net income obtained from lending ought to be separately accounted for in regular reports to beneficiaries, since it is neither appropriate to regard it as a part of investment return, nor should it be allowed to conceal the actual costs of custody, transfer, and other administrative costs, or the costs attendant upon the actual lending program itself.

10.3. Additionally, in any public report on voting decisions made during the preceding year, the instances in which shares were not voted because they were out on loan, and the resultant 'under-vote' of shares, by percentage or by actual number, ought to be disclosed to beneficiaries of the reporting funds.