

SRD II in review:

A call to action after the Call for Evidence

Nicky Dalgleish, vice president of business governance for investor communication solutions at Broadridge, discusses what the ESMA and EBA publication on SRD II means for the industry

At the end of July, The European Securities and Markets Authority (ESMA) and the European Banking Authority (EBA) handed their report on the implementation and effectiveness of the revised Shareholder Rights Directive (SRD II) to the European Commission.

Their analysis and recommendations were adapted from national regulators' opinions on ESMA's Call for Evidence. The opinions came from a total of 73 market participants, including Broadridge.

Broadridge representatives also met separately with ESMA to discuss their insights and recommendations, based on the company's extensive experience providing SRD II-compliant proxy voting and shareholder disclosure services.

Harmonisation

The ESMA and EBA report highlighted processes that would benefit from harmonisation across EU markets. It also outlined that definitions such as 'shareholder' and 'eligible securities' needed more clarification between different jurisdictions.

Respondents taking part in the report reflected that there isn't a clear industry consensus on the definition of 'shareholder'. Some 56 per cent of respondents favoured the term 'beneficial shareholder', 12 per cent preferred 'nominee shareholder' and 32 per cent said they would choose another term.



In the report, ESMA and the EBA contemplated the possibility of harmonising the definition of shareholder for ‘disclosures only’. This would be a disappointing outcome and a lost opportunity to achieve the objectives of ESMA’s Capital Markets Union plan.

The interpretation of the definitions adds complexity and cost, as intermediaries and their service providers must implement market-specific requirements into their processes. These complexities will remain if the shareholder definition is harmonised for disclosure only. In addition, assuming the definition of beneficial shareholder is chosen, it seems unbalanced to mandate the disclosure of information about beneficial shareholders in markets which won’t reciprocate this by mandating voting rights for these investors.

In any event, the report suggested publishing a list of definitions for ‘shareholder’ and ‘eligible securities’ across all markets to improve certainty. At Broadridge, we welcome this suggestion, assuming it is an interim step. We are interested to see whether the scope of SRD II will extend beyond shares in the future, as contemplated by the report.

It is also good news to see that ESMA and the EBA recommended harmonisation for proof of entitlement requirements. The antiquated ‘power of attorney’ processes currently required by many EU markets are costly to support and scale. They can also create a barrier to the effective exercise of underlying investor voting, particularly with regard to straight-through processing (STP).

Straight-through processing

In their report, ESMA and the EBA made several recommendations to improve STP of voting and shareholder disclosure. They suggested that issuers should be obligated to send golden operational records in an agreed format — to a central securities depository or first intermediary — to initiate both disclosure requests and corporate events, such as shareholder meetings.

The agreed formats would allow for STP and remove the reconciliation currently required to remove inconsistencies between announcements and requests received from different local market participants.

This is an exciting development. However, it may be a mistake to remove the ability of issuers to send these golden records, such as disclosure requests, to other intermediaries in the chain. In certain markets, there are concerns about bottlenecks at the first intermediary level — particularly while the uptake of ISO 20022 is still a work in progress.

There is also concern that the lack of choice could result in uncompetitive charges for the distribution of such records.

A promising suggestion is to introduce a regulation, rather than a directive, to mandate the use of machine-readable formats and other technical requirements of SRD II. These requirements would directly apply to market participants and would remove any risk of inconsistencies in local transpositions.

Broadridge is also excited to see ESMA's enthusiastic recognition of the value of ISO 20022, and the need for the scope of these technical requirements to be expanded to the proof-of-entitlement process, which requires significant manual intervention.

Vote confirmations and other key focus areas

In their report, ESMA and the EBA highlighted that respondents thought that vote confirmations had the most shortcomings. They noted that vote confirmations are not being provided in many markets and, where they are, they are only available in paper-based form. This is consistent with Broadridge's experience.

Recognising the mixed evidence on the effectiveness of the current voting confirmation framework and the lack of potential fixes, ESMA and the EBA recommended that the European

Commission recognise different strategies to assist asset managers with their compliance and ESG engagement, such as publishing voting records.

This would be consistent with the proxy voting disclosure regime in the US and a recent proposal published for consultation by the UK Financial Conduct Authority's Vote Reporting Group.

The report also suggests more transparency around charges relating to the transmission of voting and shareholder disclosure data and services as well as further reform of the proxy advisor industry, particularly in regard to the increase of its role in ESG.

In light of this, Broadridge expects that the oversight of proxy advisors will significantly increase.

Next steps

ESMA and the EBA's report will be adapted into a European Commission report to the European Parliament and Council.

Considering the review cycle and implementation timelines for SRD II, we expect that the next version of the directive, or regulation, will come into effect in 2025. ■

Nicky Dalgleish
Vice president of business governance for investor communication solutions
Broadridge

