Shareholders Rights Directive

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SHAREHOLDERS RIGHTS DIRECTIVE

Background

Directive (2007/36/EC) (the "Directive") known as the Shareholders Rights Directive was introduced in order to improve corporate governance in listed companies in Europe by enabling shareholders to exercise their voting rights and rights to information across borders. While the Prospectus Directive[1] focuses on the information which issuers have to disclose on admission to the market and the Transparency Directive[2] deals with, amongst other matters, information which companies are required to make available in relation to company meetings, neither deal with the shareholder voting process.

The Commission's proposal for a directive on the exercise of certain rights of shareholders in listed companies was adopted on 11 July 2007 and published on 14 July 2007[3].

The recitals to the Directive provide a useful overview of the principles which the parliament and the council wished to reflect through the implementation of this Directive and are important in interpreting the provisions of the Directive. The stated aims of the Directive are that:

- shareholders should be able to cast informed votes at, or in advance of, the general meeting, no matter where they reside;
- the possibilities which modern technology offer to make information instantly accessible should be exploited;
- shareholders should, in principle, have the possibility to put items on the agenda of the general meeting and to table draft resolutions for items on the agenda. This right should be made subject to basic rules, namely that any threshold required for the exercise of those rights should not exceed 5% of the company's share capital and that all shareholders should in every case receive the final version of the agenda in sufficient time to prepare for the discussion and voting of each item on the agenda;

[1] 2001/34/EC
[2] 2004/109/EC
[3] O.J14.07.2007L184P17

- every shareholder should, in principal, have the possibility to ask questions related to items on the agenda of the general meeting and to have them answered. The Directive proposes leaving the rules on how and when questions are to be asked and answered to be determined by Member States;

- companies should face no legal obstacles in offering to shareholders any means of electronic participation in the general meeting subject only to such constraints that are necessary for the verification of identity and the security of electronic communications; and

- good corporate governance requires a smooth and effective process of proxy voting. The Directive therefore provides that proxy holders should be bound to observe any instruction received from shareholders and that shareholders have an unfettered right under this Directive to appoint proxy holders to attend and vote at general meetings in their name.

Member States may exempt UCITS, non UCITS and co-operative societies from the provisions of the Directive.

This is a minimum harmonisation directive and therefore Member States are permitted to introduce more stringent measures if necessary to facilitate the exercise by shareholders of their rights. It will be interesting to see if the Irish Government limits itself to amending existing companies legislation to be in line with the minimum requirements imposed by the Directive or whether it will impose further obligations on companies to facilitate the exercise by shareholders of the rights provided for in the Directive.

The UK department for Business Enterprise and Regulatory Reform ("BERR") published a consultation document on the implementation of the Directive in the UK on 24 October 2008 which contained the UK's proposed draft regulations ("UK Draft Regulations") for implementation of the Directive.

Interestingly, the UK Draft Regulations apply in certain respects to private as well as listed companies. They propose that shareholders of all companies be allowed to vote by correspondence – electronic or by post – if the articles allow. They also provide that where multiple non-proxy representatives are appointed by corporate nominees to represent different beneficial shareholders in a company, these corporate representatives will be permitted to vote in different ways from one another in respect of different blocks of shares.

The rules which apply when a shareholders proxy cast votes for different shares in different ways are also amended for all companies pursuant to the UK Draft Regulations. The UK Draft Regulations propose that on a show of hands a proxy appointed by one member would have one vote and a proxy appointed by more than one member would have one vote if instructed to vote in the same way by all the members who appointed the proxy. If instructed to vote in different ways, the proxy will have one vote for and one vote against the particular resolution. Where a shareholder appoints more than one proxy, all the proxies taken together will have one vote for and one vote against the particular resolution. Finally, the UK Draft Regulations create a new statutory obligation on a proxy to act in accordance with any instructions given by the member(s) appointing him or her.

As drafted, the UK Draft Regulations apply immediately from 3 August 2009. This means that unless a company has passed an appropriate resolution at its 2009 AGM it will have to call any general meetings on 21 days notice unless it calls a general meeting to pass an appropriate resolution which is unlikely to be attractive to companies. The Department of Enterprise, Trade and Employment commenced drafting regulations to implement the Directive in August 2008. It is anticipated that the draft regulations will be released by the Department by February of this year.

The key provisions of the Directive are as follows.

ARTICLE 4 - CHAIRMANS CASTING VOTE

As the Directive requires that all shareholders be treated equally, provisions in company articles giving the Chairman a casting vote at shareholders meetings will not be permissible. Table A may need to be amended in this regard.

ARTICLE 5 - NOTICE PERIODS FOR EXTRAORDINARY GENERAL MEETINGS (EGM'S)

The minimum notice period for listed company EGM's for both ordinary and special resolutions will be 21 days instead of the current 14 days. This period can be reduced to 14 days if two conditions are met, namely that the company allows shareholders to vote by electronic means accessible to all shareholders and secondly that shareholders pass a resolution every year approving the lowering of the notice period. The resolution must be passed by a majority of not less than two-thirds of the shares represented at the meeting and may only last until the company's next AGM. Existing Irish legislation will need to be modified as it is currently only AGM's that require 21 days notice.

The Directive allows adjourned meetings to be held on shorter notice if the adjournment is for lack of a quorum and the company has to issue a second or subsequent notice of meeting, provided that no new item is put on the agenda for the meeting and there is at least 10 days between the original meeting and the date of the adjourned meeting.

One area of ambiguity with Article 5 of the Directive is the requirement that a company must offer *"the facility for shareholders to vote by electronic means accessible to all shareholders"*. It is not entirely clear what a company must do in order to offer *"the facility for members to vote by electronic means accessible to all members*". Is the requirement fulfilled where companies offer a facility for members to vote electronically via a website or where they use CREST to appoint a proxy to vote for them? BERR have invited comments on how to define *"electronic means accessible to all shareholders"*. Hopefully the Irish regulations when implemented will address this uncertainty.

The Directive also requires that Member States shall *"require the company to use such media as may reasonably be relied upon for the effective dissemination of information to the public throughout the Community".* It is hoped that the Irish regulations will expand on this requirement so that companies have certainty as to how their obligations can be fulfilled.

Pursuant to the Directive the notice of a general meeting of a listed company has to include the following:

- details of the website on which the information that must be published before the meeting is available;
- the precise procedures with which members must comply in order to be able to attend and vote at the meeting (including the date by which they must comply);
- any forms to be used to appoint a proxy;
- a statement of the members right to ask questions, to put items on the agenda and to table draft resolutions; and
- a statement that the right to vote at the meeting is determined by reference to the register of members on a particular date and that only those who are shareholders on that date shall have the right to participate and vote in the general meeting.

These requirements are in addition to the requirements regarding notices of general meetings contained in the Company's Acts 1963 – 2006, the Listing Rules and the Transparency (Directive 2004/109/EC) Regulations 2007.

The Directive also requires a listed company to publish the following information on its website before a general meeting:

- the notice of the meeting;
- the total number of shares and voting rights at the date of the notice; and
- the documents to be submitted at general meeting.

The information must be available on the website throughout the period beginning with the first date on which the notice of the meeting is sent and ending with the conclusion of the meeting.

The UK Draft Regulations clarify that failure to comply with this section does not affect the validity of the meeting or anything done at the meeting. In addition, they provide that if this section is not complied with an offence is committed by every officer of the company who is at fault and that any person guilty of an offence under the particular section of the regulations is liable on summary conviction to a fine.

ARTICLE 6-SHAREHOLDERS RIGHTS TO PUT ITEMS ON THE AGENDA AND TO TABLE RESOLUTIONS FOR THE AGM

The Directive requires Member States to ensure that shareholders have the right to:

- put items on the agenda of the general meeting, provided that each such item is accompanied by a justification or a draft resolution to be adopted in the general meeting; and
- table draft resolutions for items included or to be included on the agenda of a general meeting.

The Directive further provides that where any of these rights are subject to a condition that the relevant shareholder or shareholders hold a minimum stake in the company, such minimum stake shall not exceed 5% of the company's share capital. Member States are also obliged to set a single deadline with reference to a specified number of days prior to the

general meeting by which shareholders may exercise the right to put items on the agenda or to table draft resolutions. Where the right to put items on the agenda or to table draft resolutions entails a modification of the agenda for the general meeting which has already been communicated to shareholders, the company is obliged to make available a revised agenda in the same manner as the original agenda in advance of the applicable record date.

In the UK sections 338 to 340 of the UK Companies Act 2006 (which replace sections 376 and 377 of the Companies Act 1985) provide that members of a public company holding at least 5% voting rights or at least 100 members of a public company holding an average of £100 paid up capital have the right to propose a resolution for the AGM agenda and requires the company to circulate details of the resolutions to all members.

The UK Draft Regulations slightly amend the existing provisions by providing that member's powers to propose resolutions for AGMs applies to traded companies as well as public companies. It also inserts a new section 338A which allows members of a traded company (who represent at least 5% of the total voting rights of all the members or at least 100 members who can vote and hold shares paid up on average, per member, as to at least £100) to require the company to include a matter (other than a proposed resolution) at an AGM.

The UK Draft Regulations also amend sections 339 and 340 of the UK Companies Act 2006 to ensure that the cost of circulating resolutions for the AGM of the company is placed on the company. In Ireland, the only similar right that exists is contained in section 132 of the Companies Act 1963 which provides that members of a company holding not less than one tenth of the paid up capital of the company may convene an extraordinary general meeting of the company.

ARTICLE 7-THE ABOLITION OF SHARE BLOCKING

The Directive requires the use of a "record date" system which is already used in Ireland. On this date shareholders are validated for voting at the meeting but shares can still be traded after this date. Share blocking (whereby shareholders are required to notify the company of their intention to vote and after this date are unable to sell their shares) is to be abolished under the Directive.

Share blocking does not occur in Ireland or in the UK. However, as it is not unlawful in the UK the UK Draft Regulations are amending UK law to prohibit it. The record date may not be more than 30 days before the general meeting.

ARTICLE 8-REMOVAL OF LEGAL OBSTACLES TO ELECTRONIC PARTICIPATION

The Directive requires that Member States must not have any barriers to electronic participation in general meetings save those relating to security and identification of shareholders which can be justified proportionately. Member States are also required to permit companies to offer to their shareholders any form of participation in the general meeting by electronic means, notably any or all of the following forms of participation:

- real-time transmission of the general meeting;
- real time two-way communication enabling shareholders to address the general meeting from a remote location; and
- a mechanism for casting votes, whether before or during the general meeting, without the need to appoint a proxy holder who is physically present at the meeting.

ARTICLE 9-THE RIGHT TO ASK QUESTIONS

The Directive gives the right to every shareholder to ask questions related to items on the agenda of the general meeting. The right to ask questions and the obligation to answer those questions are subject to measures which Member States may take to allow companies to ensure the identification of shareholders and the protection of confidentiality of the business.

Member States may provide that an answer will be deemed to be given if the information can be found on the company's website. Presently the responsibility for the conduct of meetings is given to the chairman within the bounds of the company's articles of association and common law. A change in Irish law is therefore required to place an obligation on the company to answer questions.

The UK Draft Regulations do not include an exemption for the protection of the company's business interests or make it clear that one overall answer may be given to questions with the same content which the Directive permits. It will be interesting to see what position the Irish Government takes in these matters.

ARTICLE 10- PROXY VOTING

The Directive prescribes that every shareholder shall have the right to appoint any natural or legal person as a proxy holder. Other than the requirement that the proxy holder have legal capacity Member States can not impose further requirements as to the eligibility of the proxy holder. Member States are also prohibited from restricting shareholders exercising their rights through proxy holders other than to prevent a conflict of interest arising between the proxy holder and the shareholder.

The Directive creates a statutory obligation on a proxy to act in accordance with any instructions given by the member appointing him or her. Common law arguably would infer such an obligation on a proxy, nonetheless such a duty has now been given a legislative basis.

The Directive stipulates that Member States may require proxy holders to keep a record of the voting instructions that they have received from the appointing shareholder and to confirm that they have acted in accordance with instructions received. The Directive, however, does not make clear whether a vote is affected if a proxy votes other than in accordance with its instructions. Clearly it would be helpful if the Irish implementing regulations addressed this uncertainty and the question of a shareholder's remedy if it is found that the proxy holder has not acted in accordance with instructions.

As previously stated the notice of a general meeting of a traded company will have to include any forms that are used to appoint a proxy. The UK Draft Regulations require that such proxy form be available on the company's website. This potentially raises a problem in so far that a company will usually want a proxy form to be personalised so that they can identify the shareholding appointing the proxy.

The Directive provides that a proxy holder may hold a proxy for an unlimited amount of shareholders. Furthermore, a member's proxy shall have the same right as the member to speak and demand a poll at a meeting of the Company. The UK Draft Regulations have implemented the Directive so that a proxy holder will only have one vote on a show of hands irrespective of how many shareholders he is acting for (if he is instructed to act in the same way by all those shareholders). If instructed to vote in different ways however, the proxy will have one vote for and one vote against. On a poll a proxy holder can cast as many votes as he has been appointed as proxy for. Companies will need to consider whether to make any changes to their articles to ensure that they reflect this.

ARTICLE 12 - VOTING BY CORRESPONDENCE

The Directive obliges Member States to offer shareholders the possibility to vote by correspondence without appointing a proxy in advance of the general meeting. This will require changes to current law.

ARTICLE 14 - PUBLISHING POLL RESULTS ON A WEBSITE

Article 14 of the Directive requires that companies should establish for each resolution at least the number of shares for which votes have been validly cast, the proportion of the share capital represented by those votes, the total number of votes validly cast as well as the number of votes cast in favour of and against each resolution and, where applicable, the number of abstentions.

Member States may provide or allow companies to provide that if no shareholder requests a full account of the voting, it shall be sufficient to establish the voting results only to the extent needed to ensure the required majority is reached for each resolution. Companies are obliged pursuant to the Directive, within a period of time not exceeding 15 days after the general meeting, to publish on their internet site the voting results established as above.

The Combined Code's good practice standards would presumably continue to require the company to publish certain information about the results of a resolution taken on a show of hands on its website as soon as reasonably practical.

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