

2017 EUROPE AGM SEASON PREVIEW

As the 2017 AGM season gets underway, we give an overview of the key issues facing European issuers and their investors. This document accompanies our European 2017 Proxy Season Preview Podcast (see Appendix 1).

STEADY PROGRESS

At the EU level, 2017 will see steady progress on a range of corporate governance issues, with directives and regulations on the statutory audit and reporting on "non-financial" issues coming into force. Outside of the regulatory sphere, there will be a continued focus on board independence and diversity, board skills and remuneration structures. With the expected passage of an amended Shareholder Rights Directive in March 2017, certainly the focus will be on how to prepare for a future with increased reporting requirements and mandatory say on pay votes, among a host of other changes. For the 2017 AGM season, however, we turn our attention to two issues where we expect to see both progress and controversy during the 2017 season: board diversity and remuneration proposals.

BOARD DIVERSITY

With the growing use of binding gender diversity quotas in recent years, European boardrooms continue to diversify at a rapid pace. With much progress already made, issuers are also turning their attention to diversifying boards with respect to age, industry expertise and international experience. The most forward-looking companies will provide skills matrices for the board of directors, with Dutch companies leading their peers in this regard.

France

2017 is the year by which, according to the Copé-Zimmermann law, large and medium quoted companies in France would have to reach 40% female representation on their board of directors or supervisory board. Since the law passed in 2011, France has seen significant growth in women occupying board seats; since 2011 the percentage of women on boards in SBF 120 companies went from approximately 17% to 39%. While a significant number of companies have met the 40% target already, as can be surmised from the average, a few are expected to meet it at the 2017 AGM itself.

Germany

With binding quotas coming into effect for large German companies holding elections in 2016, shareholders should expect the 30% quota to be taken into account in the nominees proposed to supervisory boards with low female participation levels.

More interestingly, perhaps, is the potential for development with respect to companies' gender diversity targets. As part the law implemented last year, all companies are required to publish targets for the participation of the less

represented sex on both the supervisory and management boards. Last year, all companies set targets for achievement by the end of 2017 and, as a result, most targets for the management board were set at the current percentage of female members – even where that percentage is 0%. Over the course of 2017, shareholders should learn more about companies' intentions for developing board and management diversity in the long term.

Italy

With a binding provision regarding gender diversity already in place for several years now in Italy, Italian companies are looking at other ways to diversify. There is an increasing desire to increase so-called "passport diversity" as well as improving disclosure surrounding the diversity of skills on the board of directors. Notable examples of companies which are ahead of the curve in this regard would be Assicurazioni Generali and Snam.

Complementing gender diversity profiles, Italian banks are also required to outline the ideal composition of the board of directors, which includes the ideal skillset and professional backgrounds of those to be elected.

The Netherlands

Previously, a legal quota of 30% had been set for application by 2016. While many companies on the AEX and AMX will provide a discussion of diversity targets in the scope of a larger discussion of board composition, without legal ramifications associated with the quota supervisory boards do not see themselves as being strictly bound.

The new Dutch Corporate Governance Code, published last December, does place greater emphasis on the current state of affairs with diversity targets and requires disclosure of specific measures being taken where targets are not met. As such, we hope to see some improved disclosure among companies that have not made adequate progress.

Spain

In Spain, the focus will remain on gender diversity with companies expected to have 30% female participation by 2020. We will be looking at how companies approach this target and particularly, how they discuss the progress made so far, and the work still to be done, in the annual corporate governance report. While some companies still have a lot of ground to make up, the overall picture is somewhat positive. Within the IBEX 35 approximately 20% of board positions are currently occupied by female directors, which is in line with the current European average of 21%.

Switzerland

In November 2016, the Federal council sent a draft of the Code of Obligations forward for Parliament's approval. Included in that draft are comply-or-explain

gender quotas of 30% for board of directors and 20% for companies' executive committees.

Currently, the only requirement with respect to gender diversity in Switzerland is a comply or explain provision in the Swiss Code of Best Practice for Good Corporate Governance which only calls for boards to have both genders represented by at least one director. Therefore, while the law has not yet been approved, the suggestion of this higher requirement and particularly the executive committee quota may lead to increased scrutiny of these issues in Switzerland going forward.

SAY ON PAY

As with prior years, pay will likely remain the most controversial topic at many AGMs across the continent. Unlike previous years, few specific changes driven by regulations or corporate governance codes are expected in 2017 apart from in France and Switzerland. However, with say on pay approval rates still far below the average for other proposals in most of Europe, we expect companies to continue to make structural reforms and improve disclosure this year.

France

In 2016, for the first time the provision for a mandatory say on pay vote at listed companies was included in French law. Through a law known as "Sapin 2", France has mandated two different types of yearly binding votes on executive remuneration. The first of these, a forward-looking vote on remuneration policy, will come into force at listed companies' 2017 AGM. The second vote, on variable and extraordinary amounts paid in the preceding year, will only become applicable starting at the 2018 AGM, for most companies. What distinguished this second vote from similar provisions in Switzerland and elsewhere in Europe is that it will require that companies receive shareholder approval before disbursing variable and extraordinary pay to their executives. These provisions make the French say on pay rules the most stringent in Europe.

Looking forward to possible contentious meeting in 2017, all eyes will surely be on the Renault AGM. It was the controversy surrounding Renault's response to the failed advisory vote on the remuneration of its CEO that provided the impetus legislators needed to push through these new rules.

Switzerland

The latest version of the Code of Obligations shied away from enforcing a retrospective vote on bonus amounts – a provision that was included in previous drafts. Instead, in its current form, it calls for a retrospective, non-binding vote on the remuneration report where pay amounts are approved prospectively. Other provisions included in the newest version of the Code of Obligations appear to be intended to provide more guidance with respect to elements of executive compensation which are governed by the Swiss constitution, such as sign-on awards and severance payments. These clarifications include a cap on non-

compete agreements equal to the average compensation paid in the past three years, and a prohibition of sign-on bonuses that do not demonstrably compensate for awards forfeited from the previous employer.

OTHER DEVELOPMENTS TO WATCH

Apart from board diversity and say on pay, there are a few other notable issues to watch in the 2017 AGM season.

Audit Regulation

In EU member states, new audit regulations will take effect from this year requiring that audit firms rotate their statutory auditor after 10 years. Transitional arrangements will allow longer-serving auditors to potentially serve until 2023. Expect questions to be asked of companies that avail of the longer time horizon without explanation.

Non-Financial Reporting

As of January 2017, 11 EU member states had missed the transposition deadline for the directive on non-financial reporting. Then again, the European Commission has extended its previous deadline for providing guidance to issuers on how to implement the requirements until “as soon as possible in the spring of 2017.” Regardless, we expect most large companies that will be affected by the expanded reporting requirements on environmental, social, human rights, anticorruption and diversity issues to make some improvements in 2017. Indeed, many issuers are well ahead of the requirements by offering integrated reporting and/or sustainability reports. Still, 2017 should see more reluctant companies starting to catch up to their sustainably-minded peers.

Stewardship and Engagement

While most European markets have seen a substantial uptick in engagement between shareholders and board members, both Germany and the Netherlands have gone as far as to amend their corporate governance codes to emphasize the need for engagement and the role of investors as stewards. While not yet final, the changes to the German Corporate Governance Code, if approved, will suggest that the chairman of the supervisory board has a defined role in engaging with shareholders. Given the historic reluctance of supervisory boards to engage directly with shareholders, we may see an uptick in activity in 2017 as potentially controversial issues arise.

APPENDIX 1

The Proxy Season Preview Podcast accompanying this document may be found at <http://www.glasslewis.com/blog/>.

Show Notes

- Steady progress on governance initiatives in the EU. (0:50)
- How boards are evolving in Europe. (4:00)
- German gender quotas and targets: are they working? (4:30)
- Switzerland lags in board gender diversity, but may be catching up. (6:40)
- Dutch companies fail to meet diversity targets. (7:32)
- France charges ahead on diversity, including executive pipelines. (8:10)
- Progress on diversity is picking up in Spain. (9:59)
- How companies are assessing board profiles and skills. (11:25)
- Dutch companies detail supervisory board profiles well. (12:30)
- Italian companies merge internal board evaluations with disclosure. (13:20)
- The *voto di lista* provides proxy access in Italy, with a twist. (14:30)
- The lead director becomes independent in France. (16:33)
- Say on pay is still the center of attention. (17:37)
- France mandates *formidable* binding pay votes. (18:05)
- Swiss pay amounts under scrutiny. (19:59)
- French shareholders not likely to be shy in voicing opposition to high pay. (22:18)
- New say on pay requirements in the Shareholder Rights Directive. (23:30)
- German and Dutch companies focus on pay policy amendments. (24:45)
- A few high-profile meetings in Europe with regard to pay. (26:48)
- Turning our attention to non-financial reporting. (30:00)
- Who is leading the way on non-financial reporting? The Dutch? Italians? The French? (31:59)
- Engagement and stewardship. (37:01)
- The Dutch and German Corporate Governance Codes focus on engagement. (38:00)
- An update on Italian shareholder stewardship efforts. (41:04)
- Surveying French shareholders on stewardship. (42:49)
- Glass Lewis presents 2017 policy updates. (44:43)

APPENDIX 2

Selected links from the Proxy Season Preview and Podcast.

The following policy positions, corporate governance recommendations and legal updates were updated in 2016 and referenced in the podcast.

- Revisions to the Shareholder Rights Directive
<http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2014:213:FIN>
- Statutory Audit Regulation and Directive
<http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32014R0537>
- Non-Financial Reporting Directive
<http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014L0095>
- Dutch Corporate Governance Code revisions
<http://www.mccg.nl/?page=3779>
- Proposed revisions to the German Corporate Governance Code
<http://www.dcgk.de/en/consultations/current-consultations.html>
- Afep Medef Corporate Governance Code revisions
<http://www.afep.com/uploads/medias/documents/Code%20de%20gouvernement%20d'entreprise%20des%20soci%C3%A9t%C3%A9s%20cot%C3%A9es%20novembre%202016.pdf>
- Copé-Zimmerman law on balanced gender representation on boards
<https://www.legifrance.gouv.fr/affichTexte.do?cidTexte=JORFTEXT000023487662&dateTexte=&categorieLien=id>
- Loi Sapin 2
https://www.legifrance.gouv.fr/affichTexte.do;jsessionid=A9B5AB6EB56348B97E6E3DE06ACDC7E.tpdila17v_3?cidTexte=JORFTEXT000033558528&categorieLien=id

Further information on Glass Lewis.

- Glass Lewis 2017 Policy Guidelines
<http://www.glasslewis.com/guidelines/>
- Glass Lewis engagement policy
<http://www.glasslewis.com/engagement-policy/>
- Meetyl engagement platform
<https://meetyl.com/>