ARTICLE

Shareholders Holding the Reins on Remuneration: The European Say on Pay

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1. INTRODUCTION

Over the last decade, executive remuneration developed into the most debated topic in corporate governance. In the earlier days of corporate governance, the composition of an executive remuneration package was considered the key mechanism aligning the interests of the top management and executive board members and the shareholders of the company. According to this 'optimal contracting theory' the level and composition of the pay package reflects the market equilibrium for managerial talent, effectively optimizing firm value. The structure and size of the remuneration package serve as the mitigating instrument of the agency conflict between executive board members and top management and the shareholders.[1] However, this theory has been challenged. Management is very powerful in remuneration negotiations and extracts rents from shareholders. Not only the composition of the pay package, but also the level of remuneration is not the result of market forces but is determined by rent-seeking managers. Compensation consultants, stealth compensation, severance payments and at-the-money options are hereby used to shift wealth from companies to executive directors. Bebchuk and Fried defend this 'managerial power theory' fiercely and argue that an external outcry is an important technique to halt the extracting rent behavior.[2] In short, while the 'optimal contracting theory' considers the remuneration package as a solution for an agency problem, the 'managerial power theory' argues that executive compensation is a symptom of the agency problem.

While research finds support for both theories,[3] pay packages and especially remuneration levels did not go unnoticed in parliaments and governments. In many countries, the government stepped in to address the composition of top pay and sometimes even the level of compensation which is assumed to be overly excessive. Whilst the arena of executive compensation was dominated by the board of directors and management, governments introduced, as a first step of enhanced corporate governance, the right for shareholders to be informed of the remuneration packages of managers.[4] More recently, this disclosure of pay is no longer seen as sufficiently balancing the powers of the shareholders and the board of directors and in recent corporate governance codes and regulatory initiatives shareholders are empowered to voice the compensation of the executive board members and top management.[5] In the next sections, we will address the state of the art regarding say on pay at the level of the European Union. The European Commission played a significant role in advancing shareholder rights and in the recent modernization of the Shareholder Rights Directive, say on pay will become part of the European *acquis*. First, we provide in a short historical overview of European developments of say on pay.[6] Next we analyse the new say on pay regime that the Directive implements. We conclude that while this development is a major step forward towards more shareholder empowerment, the effects of say on pay on compensation (levels) must not be overstated.

2. EARLY DEVELOPMENTS OF SHAREHOLDER INVOLVEMENT IN EXECUTIVE PAY

The current European viewpoints to provide shareholders more influence in the setting of top executive pay is based on a discussion that started over a decade ago. In its 2003 Communication on 'Modernising Company Law and enhancing Corporate Governance

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1 K. Murphy, *Executive Compensation: Where We Are, and How We Got There*, in *Handbook of the Economics of Finance*211, 212 (George Constantinides, Milton Harris & Rene Stulz eds, 2012).

2 L. Bebchuk & J. Fried, *Pay Without Performance, The Unfulfilled Promise of Executive Compensation* (London: HUP 2004).

3 C. Frydman & D. Jenter, *CEO Compensation*, Ann. Rev. Fin. Econ. 75–102 (2010).

4 *See* e.g. the Dutch disclosure requirements in Art. 2:383c Civil Code, introduced in 2003.

5 R. Thomas & C. Van der Elst, *Say on Pay Around the World*, 92 Wash. U. L. Rev. 653–731 (2015).

6 An overview of the European regulatory developments of executive pay can be found in C. Van der Elst & M. van Falier, *The European Remuneration Framework: Recent Policy Changes and Their Implications on Executive Remuneration Contracts*, in *Executive Directors' Remuneration in Comparative Corporate Perspective* 13–48 (C. Van der Elst ed., Alphen aan den Rijn: Kluwer Law International 2015).

Van der Elst, Christoph. 'Shareholders Holding the Reins on Remuneration: The European Say on Pay'. *European Company Law Journal* 14, no. 3 (2017): 114–120.

in the European Union – A plan to move forward'[7] the European Commission considered that the shareholders must be provided with an approval right for directors' share and share option schemes, one of four key remuneration items.[8] The Commission based its consideration on the 2002 recommendations of High Level Group of Company Law Experts, an ad hoc advisory group of experts, who first had a role in providing solutions for the then by the European Parliament rejected Takeover Directive. The experts' group mandate was extended to also provide in recommendations for modernizing company law and corporate governance.[9] The recommendations not only included the aforementioned approval right for share (option) schemes but also the advice for organizing a shareholder debate on the remuneration policy for directors which should be disclosed. At that time, the experts did '*not believe a shareholder vote on the remuneration policy generally should be an EU requirement, as the effects of such a vote can be different from Member State to Member State*'.[10] It was a response on the developments in the United Kingdom where a rule of a mandatory but advisory vote on the remuneration report was pending.[11]

The European Remuneration Recommendation of 2004[12] did not only contain the rules the Commission already communicated in 2003 but also provided in some explicit say on pay recommendations that went well beyond the High Level Group's advice. According to Article 4.1. of the Recommendation the general meeting of shareholders should be provided with an advisory vote on the remuneration policy as well as on the significant changes to this policy. Article 4.2. of this Recommendation wants companies to grant shareholders an advisory or binding vote on the remuneration statement. The latter vote can be made dependent upon the request of the shareholders representing more than 25% of the votes present or represented at the general meeting.[13] The difference between the remuneration policy and the remuneration statement was not entirely clear. According to Article 3.1. the remuneration statement is the '*statement of the remuneration policy of the company*'. Article 3.2. of the recommendation continues that the statement '*should mainly focus on the company's policy on directors' remuneration for the following financial year and, if appropriate, the subsequent years'*. However the statement goes beyond the policy and must contain information related to the remuneration package of the directors including:

(1) an explanation of the relative importance of the variable and non-variable components of directors' remuneration;
(2) sufficient information on the performance criteria on which any entitlement to share options, shares or variable components of remuneration is based;
(3) sufficient information on the linkage between remuneration and performance;
(4) the main parameters and rationale for any annual bonus scheme and any other non-cash benefits; and
(5) a description of the main characteristics of supplementary pension or early retirement schemes for directors.[14]

The statement should also disclose information related to the terms of the contracts of the directors and the decision making process for setting the remuneration policy of the directors.[15] Finally, the statement must inform the shareholders of the composition and mandate of the remuneration committee.[16]

The Recommendation is firm with respect to the share based remuneration which must be approved by the general meeting. The approval must relate to:

(1) grant of share-based schemes, including share options, to directors;
(2) the determination of their maximum number and the main conditions of the granting process;
(3) the term within which options can be exercised;
(4) the conditions for any subsequent change in the exercise price of the options, if this is appropriate and legally permissible;
(5) any other long term incentive schemes for which directors are eligible and which is not offered under similar terms to all other employees.[17]

In July 2007, the European Commission issued a report on the application of the Commission Recommendation of 2004. It found that the advocated say on pay of the recommendation '*does not seem to be appropriately implemented in the majority of Member States*'.[18] Only eight countries, or one out of every three European Member States, implemented the best practice of a shareholder approval of

7 COM (2003) 284 final (Brussels 21 May 2003).
8 *Ibid.*, at 16. The other three being: the disclosure of the remuneration policy in the annual accounts, the disclosure of details of remuneration of individual directors in the annual accounts, and proper recognition in the annual accounts of the costs of such schemes for the company.
9 The High Level Group of Company Law Experts, *A Modern Regulatory Framework for Company Law in Europe* (Brussels 4 Nov. 2002).
10 *Ibid.*, at 64.
11 For an overview of the U.K. developments *see* Thomas & Van der Elst, *supra* n. 5, at 664–669.
12 European Commission, Commission Recommendation of 14 Dec. 2004 fostering an appropriate regime for the remuneration of directors of listed companies, O.J. (L 385) 29 Dec. 2004, 55 (EC).
13 Next to the existing national rules allowing shareholders to add an item on the general meeting of shareholders.
14 Art. 3.3. of the Recommendation.
15 Art. 3.4. of the Recommendation.
16 *Ibid.*
17 Art. 6.2. of the Recommendation.
18 European Commission Staff, *Report on the Application by Member States of the EU of the Commission Recommendation on Directors' Remuneration*, 6 (Brussels, SEC(2007) 1022, 13 July 2007).

the remuneration policy. This number should also be considered as an overestimation. France considered its vote of the annual report of being a vote including the remuneration policy. Approving the annual report can hardly be considered a vote of the remuneration policy. French companies were not obliged to disclose in detail the remuneration policy in the annual report[19] and even if companies provided the remuneration policy in the report, a vote of the annual report is not aiming at the approval of the remuneration policy. A similar remark goes for Ireland.

The financial crisis that started in 2007 shifted the interests for the involvement of the shareholders in the remuneration practices of top executives and directors towards the financial industry. In April 2009 the European Commission issued a Recommendation on remuneration policies in this sector, but it did not contain any involvement of the shareholders.[20] However at the same moment, the European Commission also continued to take the remuneration practices in other types of commercial and industrial companies serious and provided in a complementing Recommendation on the remuneration.[21] While it could have been expected that the Commission would encourage the Member States to provide in a say on pay of the remuneration policy in light of the low compliance it noticed in the 2007 staff report, it only indirectly emphasized the importance of some say on pay. In Article 6.1. of the Recommendation the Commission encourages the shareholders to attend the general meeting and make '*considered use of their votes regarding directors' remuneration, while taking into account the principles included in this Recommendation, Recommendation 2004/913/EC and Recommendation 2005/162/EC*'.

After the publication of the update of the Recommendation, the European regulatory framework is evolving at a slow pace. In April 2011, the European Commission issued a green paper on the future of the EU corporate governance framework.[22] One of the questions that were raised concerned 'Say on Pay'. It asked: '*Should it be mandatory to put the remuneration policy and the remuneration report to a vote by shareholders?*' This question offered only limited degrees of differentiation for respondents since it was limited to a mandatory vote on both the corporate remuneration policy and the remuneration report. A small majority of the respondents to the questionnaire supported holding a mandatory vote but only of an advisory nature.[23] Their answers unfortunately provided no indication as to whether they preferred forward looking Say on Pay (a vote on the remuneration policy) or backward looking Say on Pay (a vote on the remuneration report).

In its December 2012 Communication,[24] the European Commission revealed that it would make a shareholder vote on both the remuneration report and the remuneration policy mandatory,[25] probably through a modification of the Shareholder Rights Directive.[26] At the same time, the Commission would enhance the accountability of the shareholders vis-à-vis the company through the introduction of disclosure requirements for institutional investors.[27] Also, it would assess if the institutional investor's use of proxy advisor's voting services can sufficiently take into consideration the idiosyncratic characteristics of European listed companies in particular regarding the remuneration policy.[28]

3. SAY ON PAY IN THE MODERNIZED SHAREHOLDER RIGHTS DIRECTIVE

3.1. The 2014 European Commission's Proposal

In April 2014 the proposal for the modernization of the European Shareholder Directive was issued.[29] The European Commission proposed to have the remuneration policy of public listed entities 'as regards directors' approved by the shareholders at least every three years. The policy must be clear, understandable, in line with the business strategy, the values and the long-term interests of the company and structured as to avoid conflicts of interests. The policy

19 It is also stated in the report of the European Commission Staff (9) that regarding the disclosure of the remuneration the 'French law requires that the fix and variable elements of the remuneration of directors, the underlying criteria of their calculation and engagements made by the company for the benefit of directors are described in the annual report' which is not the same as the disclosure of the remuneration policy.

20 Commission Recommendation of 30 Apr. 2009 on remuneration policies in the financial services sector, O.J. (L 120) 15 May 2009, 22 (EC). Remuneration continued to be a key feature of the corporate governance developments in the financial industry. For an analysis of these developments *see* T. Dijkhuizen, *The EU's Approach to Banks' Executive Remuneration*, in *Executive Directors' Remuneration in Comparative Corporate Perspective* 49–68 (C. Van der Elst ed., Alphen aan den Rijn: Kluwer Law International 2015).

21 Commission Recommendation of 30 Apr. 2009 complementing Recommendations 2004/913/EC and 2005/162/EC as regards the regime for the remuneration of directors of listed companies, O.J. (L 120) 15 May 2009, 28 (EC).

22 *Commission Green Paper, The EU Corporate Governance Framework*, at 23, COM (2011) 164 final (5 Apr. 2011). The Action Plan follows on two Commission's recommendations and follow-up reports on the remuneration of the board of directors in which a vote on say on pay was recommended. Commission Recommendation 2004/913 of 14 Dec. 2004 Fostering an Appropriate Regime for the Remuneration of Directors of Listed Companies, O.J. (L 385) 55-59 (EC); Commission Recommendation 2009/384 of 30 Apr. 2009 on Remuneration Policies in the Financial Services Sector, O.J. (L 120) 22–27 (EC).

23 *Feedback Statement – Summary of Responses to the Commission Green Paper on the EU Corporate Governance Framework* 10 (2011).

24 *Communication of the Commission: Action Plan: European Company Law and Corporate Governance – A Modern Legal Framework for More Engaged Shareholders and Sustainable Companies* 18, COM (2012) 740 final (12 Dec. 2012).

25 *Ibid.*, at 9.

26 Directive 2007/36, of the European Parliament and of the Council of 11 July 2007 on the Exercise of Certain Rights of Shareholders in Listed Companies, 2007 O.J. (L 184) 17–24 (EC).

27 *Communication of the Commission*, *supra* n. 24, at 8.

28 *Ibid.*, at 10.

29 *Commission Proposal for a Directive of the European Parliament and of the Council Amending Directive 2007/36/EC as Regards the Encouragement of Long-Term Shareholder Engagement and Directive 2013/34/EU as Regards Certain Elements of the Corporate Governance Statement*, COM (2014) 213 final (9 May 2014), eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2014:2013:FIN.

is binding and companies shall 'only pay remuneration to their directors in accordance with a remuneration policy'. It should the maximum amounts that can be paid and shall explain how the pay and employment conditions of employees of the company were taken into account, the ratio between directors' and employees' pay and why this ratio is considered appropriate. The draft Directive contains many details as to the composition of the remuneration package as well as the information that must be disclosed.[30] The remuneration report, with detailed information on the remuneration package of directors, should, every year, be a voting item of the general meeting of shareholders.[31] Equally, the report must be clear, understandable and provide in a comprehensive overview of the remuneration package. In case the remuneration report is disapproved, the company must explain in the subsequent report how it addressed the opposition of the shareholders.

3.2. The European Parliament's Amendments

Since 2014 this proposal is debated and the European Parliament published their intermediary compromise in July 2015. The original proposal was significantly amendment to fit better into the corporate legal structure of many Member States but it hollowed the straightforward choice for this new shareholder right.

First, the amendments made it clear that the *company* establishes the remuneration policy that the general meeting of shareholders must bindingly approve, while leaving it open who in the company is responsible for establishing the policy.[32] In its original proposal the shareholders had a right to vote on the policy but it only indirectly followed from the proposed Article 9a that the company must have a policy. Further the European Parliament's proposal clarified the vote must take place at the general meeting of shareholders. Also, the Parliament's version requires that every change of the remuneration policy needs the approval of the shareholders, which was not required in the Commission's 2014 version. The Parliament maintained the obligation that at least every three year the remuneration policy is approved. Likely, it took into account that in many companies the shareholder base changes drastically in a three-year period.

Next, a fundamental amendment in the 2015 proposal is the admittance to having the general meeting approving the remuneration policy with an advisory vote. There is no information in the recitals that can explain why the Parliament has eased this requirement. Regarding the composition of the remuneration package, the Parliament added that companies should consider corporate social responsibility as performance criteria for the variable part of the remuneration package. Further, share-based remuneration should not represent the most significant part of the variable remuneration unless there is a well-reasoned explanation in the remuneration policy that this remuneration item contributes to the long-term interests and sustainability of the company. The Parliamentary draft also contains a further specification of the content of the policy regarding the pension and retirement schemes.[33]

Regarding the process of setting the remuneration policy, the latter shall explain the decision-making part. In particular, the policy shall specify the role and functioning of the remuneration committee on that matter.

Third, while the European Parliament significantly amended the Commission's proposal vis-à-vis the remuneration policy, it remained more reserved regarding the remuneration report requirements. However, like for the remuneration policy, the Parliament also relaxed the vote for the remuneration report in an advisory one. Next, when the shareholders vote against the remuneration report, the company must start up a dialogue with the shareholders for identifying the reasons of the rejection of the report, '*where necessary*'. There is no interpretation of the 'necessity' provision and neither does the Parliamentary draft indicate how the dialogue with the shareholders should be structured. According to our study, it is common for companies experiencing significant opposition of the shareholders for the remuneration report, to discuss the results of the vote with its major shareholders.[34] However, the proposal requires a '*dialogue with the shareholders*' limited to the identification of the reasons for the rejection which is, on the one side, broader than the current practices as only major shareholders are contacted in the aftermath of a rejected report while, on the other side, being more limited as sometimes also other parties, like proxy agencies are contacted and only the reasons for rejection need to be identified and current practices show that in some cases all major remuneration concerns of shareholders are discussed.

3.3. The Interinstitutional Agreement Leading to the Directive

Early December 2016, under the Slovak presidency, the Council, the Commission and the Parliament reached an agreement on the compromise of the Directive.[35] The Committee on Legal Affairs of the European Parliament approved the compromise and the European Parliament voted the draft Directive in March 2017. Finally the European Council adopted the Directive on 3 April 2017.[36]

30 The content of which we discuss when we report the modifications envisaged by the different amendments reaching for a political compromise.
31 *Ibid.*, Art. 9a, Art. 9b.
32 For the remuneration report it was made clear in the 2014 proposal that the company draws up the report, for the policy nothing was provided.
33 Art. 9a, §3.
34 C. Van der Elst, *Answering the Say for No Pay*, in *Innovations in Corporate Governance* (S. Watson & P.M. Vasudev eds, Cheltenham: Edward Elgar 2017, in press).
35 *Proposal for a Directive of the European Parliament and of the Council on Amending Directive 2007/36/EC as Regards the Encouragement of Long-Term Shareholder Engagement and Directive 2013/34/EU as Regards Certain Elements of the Corporate Governance Statement* (Brussels 13 Dec. 2016), nr. 15248/16 DRS 50 CODEC 1828, http://data.consilium.europa.eu/doc/document/ST-15248-2016-INIT/en/pdf (accessed 15 Apr. 2017).
36 http://www.consilium.europa.eu/en/press/press-releases/2017/04/03-shareholder-rights-eu-companies/ (accessed 15 Apr. 2017).

The compromise further clarifies a number of options which the European Parliament had approved in its July 2015 draft.

3.3.1 *The Remuneration Policy*

First the remuneration policy must be submitted to a vote. However, the policy vote can be of a binding or an advisory nature. The vote must be organized after every material change[37] and in any case at least every four years. This timeframe is less stringent than the one in the previous drafts where a triennial vote was supported.[38] The option for providing in a less intrusive advisory vote is maintained. Recital 28 of the Directive contains an explanation of the shift towards the advisory vote. According to the recital, the form and structure of the remuneration '*are matters primarily falling within the competence of companies, its relevant boards, shareholders and, where applicable, employee representatives*'. The compromise takes into account the current procedures in some Member States where the shareholders do not have the final say in the compensation but the (supervisory) board, with or without employee representatives. Depriving this board completely of its power regarding the remuneration and shifting it to the shareholders when providing the meeting with a binding vote, is considered too intrusive.

The choice of the Member States for an advisory or a binding vote has consequences for the application of the remuneration policy. In case there is a binding vote, the rejection of the remuneration policy results mandatorily in the application of the formerly approved remuneration policy and a resubmitting of a revised policy at the next general meeting. In case no policy had been formerly approved, the existing practices to pay the directors shall remain applicable. As long no remuneration policy has been accepted, the company can remunerate its directors in accordance with its existing practices. In case there is an advisory vote of the remuneration policy, companies shall only pay directors in accordance with a policy submitted to a vote, independent from the approval or rejection of the policy by the shareholders. A rejected policy must be revised and resubmitted at the next general meeting. The company must submit the policy to an advisory vote for being allowed to pay its directors. The voted policy will be applied even if it is rejected, while in a binding voting system the rejection of the policy results either in the application of existing practices or the application of the former policy.

Every remuneration policy must contribute to the business strategy, long-term interests and sustainability of the company and provide in an explanation how the policy contributes to those objectives. For a second time, a European rule is emphasizing that (some of) the interests of the company should be put first. Previously, the Takeover Directive requires that Member States guarantee from the board of directors to '*act in the interests of the company as a whole*'.[39] According to recital 16, it is not allowed to relate pay entirely or mainly to short-term objectives. This condition is not reneged in the proposed Directive but the specification that the policy must contribute to the long-term interests of the company makes it unlikely that remuneration packages exclusively or mainly linked to short-term objectives can be in compliance with the long-term interests of the company. The policy must also be clear, understandable and describe the different components of the fixed and variable remuneration. It is not uncommon that a European directive provides in the requirement to make use of 'clear and understandable' language[40] but it remains an open question which terminology will be compliant with the Directive knowing that many current remuneration packages are very complex.

Derogations from an approved remuneration policy are only allowed in exceptional circumstances which must serve the long-term interests and sustainability of the company or assuring its viability and in accordance with the procedural provisions in the remuneration policy to derogate from this policy. In that case, the remuneration report must contain information '*on the remuneration awarded under such exceptional circumstances*'.[41]

The Directive elaborates on a number of items that the remuneration policy must address. First, the remuneration policy must explain how the pay and employment conditions of employees of the company are taken into account for the remuneration policy of the directors. It relaxes the 2014 proposal of the Directive whereby the company had to provide in the ratio of the average remuneration of directors to the average remuneration of full time employees and explain the appropriateness of this ratio.[42]

Second, the policy must set '*clear, comprehensive and varied criteria*' for awarding variable remuneration. The latter criterion – variable remuneration must be based on varied criteria – includes the use of both financial and non-financial performance criteria. The Directive does not provide any guidance as to the relative

37 There are sometimes conflicts between shareholders and boards as to the qualification of 'material'. E.g. on whether a change in the composition of the peer group for comparing corporate performance is submitted to a vote, *see* C. Van der Elst & A. Lafarre, *Shareholder Voice on Executive Pay: A Decade of Dutch Say on Pay*, 1 Eur. Bus. Org. L. Rev. 1–33 (2017), doi:10.1007/s40804-017-0065-3.

38 It is not clear why during the adopting process the timeframe increased to four years.

39 Art. 3 (1) of Directive 2004/25/EC of the European Parliament and of the Council of 21 Apr. 2004 on takeover bids, O.J. (L 142) 30 Apr. 2004, 12 (EC).

40 *See* e.g. Art. 69 of the UCITS IV Directive: 'The prospectus shall include, independent of the instruments invested in, a *clear and easily understandable* explanation of the fund's risk profile' (Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), O.J. (L 302) 17 Nov. 2009, 32 (EC)).

41 Recital 30 of the Directive of the European Parliament and of the Council on amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement (Brussels 27 Mar. 2017), PE-CONS 2/17 DRS 2 CODEC 31, http://data.consilium.europa.eu/doc/document/PE-2-2017-INIT/en/pdf (accessed 15 Apr. 2017).

42 This requirements exists in the United States. Following up on s. 953 of the Dodd-Frank Act, The US SEC issued a rule of pay ratio disclosures in Aug. 2015, effective from 2017 onwards (https://www.sec.gov/news/pressrelease/2015-160.html (accessed 15 Apr. 2017).

weight of both financial and non-financial criteria and neither does it include any advice as to the appropriate financial performance criteria. For non-financial performance criteria the Directive adds that the criterion of corporate social responsibility should be included, where appropriate. In recital 29, the relevant non-financial criteria are '*environmental, social and governance factors*'. The Directive does not clarify the wording 'where appropriate'. I am of the opinion that companies cannot leave out no non-financial criteria considering that at the company level these criteria are 'not-appropriate'. Whether it can exclude individual or categories of directors is less obvious. I believe that the appropriateness of using non-financial criteria should be tied to the duties and functions of the directors. In all circumstances the company must explain how the criteria will contribute to the business strategy, long-term interests and sustainability of the company. When part of the remuneration package is variable, the company must explain in the remuneration policy the methods determining to which extent the criteria have been reached. The policy must certainly identify any deferral periods when granting variable remuneration as well as any clawback that is installed.

Third, for share-based remuneration, the policy must specify the vesting periods, the retention periods and the explanations how this type of remuneration contributes to the business strategy, long-term interests and sustainability of the company.

Fourth, the company must specify the duration of contracts and other arrangements with the directors as well as any notice periods, terms and payments linked to termination. Related to the termination of the relationship with the company, the policy must also indicate what the main characteristics of the supplementary pension schemes and other early retirement schemes are.

Finally, the policy must clarify the process for establishing the remuneration policy. According to the Directive there are three steps in the process that need explanation: the determination of the policy, its review and its implementation. Every time the policy will be revised, the revising process must be documented: the changes that will be made, the votes and views of the shareholders and the consecutive remuneration reports. This approach can be at odd with the timeline: when a remuneration policy is amended while the previous policy was approved by the overwhelming majority of the shareholders, the views of the shareholders are that they supported the current policy which, however, will be amended. Reporting the shareholders' views on the previous policy is therefore superfluous. Reporting the views of the shareholders on the proposed new policy which still needs approval seems premature: it requires that (some?) shareholders are contacted before the policy is made public. It must be made compliant with the basic rule of 'equal access to information' in the Market Abuse Regulation.[43]

When reporting the process, the policy must also explain how it mitigates and manages conflicts of interests and which role the remuneration committee played in the development, review and implementation of the remuneration policy.

In some of the Member States, the remuneration policy already must be submitted to the general meeting of shareholders. This is for instance the case in the Netherlands and the UK. In the latter country, the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 introduced specific rules related to the content of the remuneration policy. It is obvious that some of these rules can be found in the Directive although many others are not, while other parts have been adapted. Both sets of rules, the UK Regulation and the European Directive require the policy to contain a description of each of the components of the remuneration package. An item of which the UK rule requires appropriate information is the particular arrangement specific to any director to be disclosed in the policy. The Directive is silent about this item. Finally, while the proposed Directive requires the policy to be contributing to the business strategy, long-term interests and sustainability of the company, the UK-rule sounds that each component of the remuneration should support '*the short and long-term strategic objectives of the company*'.[44]

3.3.2 *The Remuneration Report*

Article 9b of the Directive calls for a yearly advisory vote on the remuneration report. For small and medium-sized companies the vote can be replaced by providing the remuneration report as a discussion item at the general meeting of shareholders if the Member States provide in this option. Like the policy, the remuneration report must be clear and understandable and provide in a comprehensive overview of the remuneration of the directors of the past financial period per individual director. We are of the opinion it is regretful that the information is limited to the last accounting period as provided at the start of the first paragraph of Article 9b of the Directive and does not provide in a comparison with the previous accounting period. However, later the Directive requires reporting of the annual change of the remuneration over a period of five years.

For each remuneration component the report must provide the total amount. It should also report on the relative proportion of fixed and variable remuneration. The Directive does not indicate which component should be considered as fixed and which component is variable which is not always obvious as it is the case for pension benefits. The report must also show how the total remuneration of the director complies with the policy and how it contributes (only) to the *long-term performance* of the company. It is difficult to see how this requirement can be harmonized with the

43 Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 Apr. 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC, O.J. (L 173) 12 June 2014, 1 (EC).

44 The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013, Part 4, 26.

remuneration policy that must make sure that the combined business strategy, the long-term interests and the sustainability is incorporated in the remuneration policy. The report shall explain how the criteria have been applied.

The report shall also present the evolution of the remuneration of the directors, the performance and the wage of the employees in a comparable manner. While the Directive requires to make use of '*the full-time equivalent basis of the employees of the company other than directors*',[45] it is silent as to which performance criterion and which remuneration of the directors must be used in the comparison.

For each director any other remuneration of companies of the group must be provided, as well as the number of shares and share options including the main conditions and clawback regimes. In case the remuneration deviates from the policy, the company shall explain the exceptional circumstances causing the derogation. The European Commission is authorized to provide in guidelines for a harmonized presentation of all the remuneration related data.

The Directive takes into account privacy issues. The information must be held available for a period of ten years from the publication onwards. Any longer period can be provided by the Member States if the personal data of directors are removed. In any case, no information of the director that reveals racial or ethnic origin, political beliefs, trade union membership, genetic data etc. shall be disclosed.

4. CONCLUSION

The developments towards more say on pay cannot be stopped. In many European countries, including the UK, Sweden, the Netherlands, Belgium and Italy a system of say on pay is already legally provided. France is the last in this row with the 'Loi Sapin II' of 9 December 2016 requiring a mandatory vote on the remuneration policy. Also the European Union considers it important that shareholders are not only aware of the remuneration packages of the executive board members, but can also influence these packages through the vote of the remuneration policy and the remuneration report. The harmonization efforts at the European level can be supported.[46] Currently, there exists as many systems of say on pay as there are countries in the European Union, while it can hardly be argued that the remuneration policy and packages of top executives are, by nature, so different between the different countries that no harmonization of the regulatory framework is necessary.

However, the harmonization efforts shall obviously not stop the debate for an appropriate remuneration package of top executives. In the UK, one of the few countries with a vote on both the remuneration report and the remuneration policy, the debate on executive remuneration levels is all but over. In fact, in 2016 the highest pay ever was noted[47] raising questions as to the need to 'cap bosses' pay'.[48] An option to address this issue could be to include in the remuneration policy, an item that discusses the maximum level of remuneration. As far as we could ascertain, there are no clear guidelines yet addressing this remuneration item. It should also be noted that there are cases where it is proven that the remuneration policy caps the pay packages: in 2016 the CEO of AB Inbev and the top management team received no variable pay as the performance criteria were not met, while the total bonus for 2015 was close to EUR 15 mio.[49]

While being a major step forward for shareholder empowerment, shareholder can only approve or disapprove the whole remuneration policy and the whole remuneration report. When disapproving the policy and/or the report, a difficult tasks of investigation the reasons for the disapproval is bestowed upon the board. It could therefore be helpful that the right of the shareholders to vote for the policy and the report is accompanied with a duty to disclose to the company the reasons for disapproving these voting items, signalling the major arguments for this opposition which can be helpful in overcoming this part of the agency conflict.

45 Also this specification will result in interpretation problems: must all employees be taken into account, what if the company does not employ employees (holding company), must foreign employees be taken into account, does the remuneration need to take into account social security costs or taxes, etc.

46 *See also* Van der Elst & Lafarre, *supra* n. 37, at 33.

47 For the CEO of WPP, https://www.wsj.com/articles/wpp-ceo-martin-sorrell-receives-103-million-in-compensation-for-2015-1461941572 (accessed 28 Feb. 2017).

48 C. Cornish & J. Pickard, *Shareholders Demand Right to Cap Bosses' Pay*, Fin. Times FM 10 (27 Feb. 2017).

49 J. Cardinaels, *Geen Bonus voor Brito na slecht 2016*, De Tijd (3 maart 2017).