



# **Market Discipline and Regulation**

## **A Survey by SWIPRA**

2015



# SWIPRA Survey

- Corporate Governance Survey 2015 participants
  - All SPI® companies
  - Swiss institutional investors, pension funds and asset managers
  - International institutional asset managers
- In cooperation with researchers at the DBF (UZH)
- Special thanks to:
  - the Pension Fund of Credit Suisse Group (Switzerland) and

**D.F. KING**

**FINANZ** und  
**WIRTSCHAFT**

**SFAMA**

 Swiss Funds &  
Asset Management  
Association



Swiss Exchange

**PETRANIX**   
Corporate and Financial Communications



**SHERPANY**  
EMPOWERING BOARD & SHAREHOLDERS

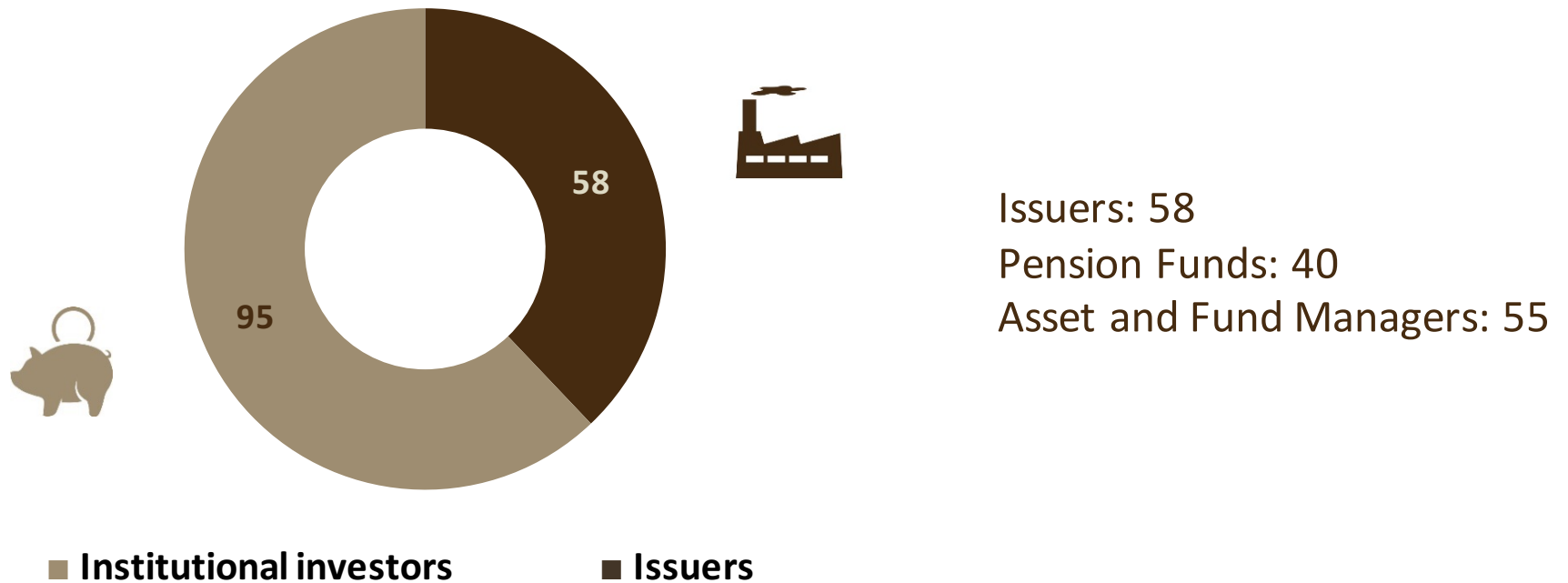


## Plan for this presentation

- **Basic information on the survey**
- Key results
- Agenda items: relevance and effort
- Disclosure: quality and quantity
- Shareholder voting rights: benefits and costs
- Regulation: hopes and fears
- Summary and outlook



# Participants

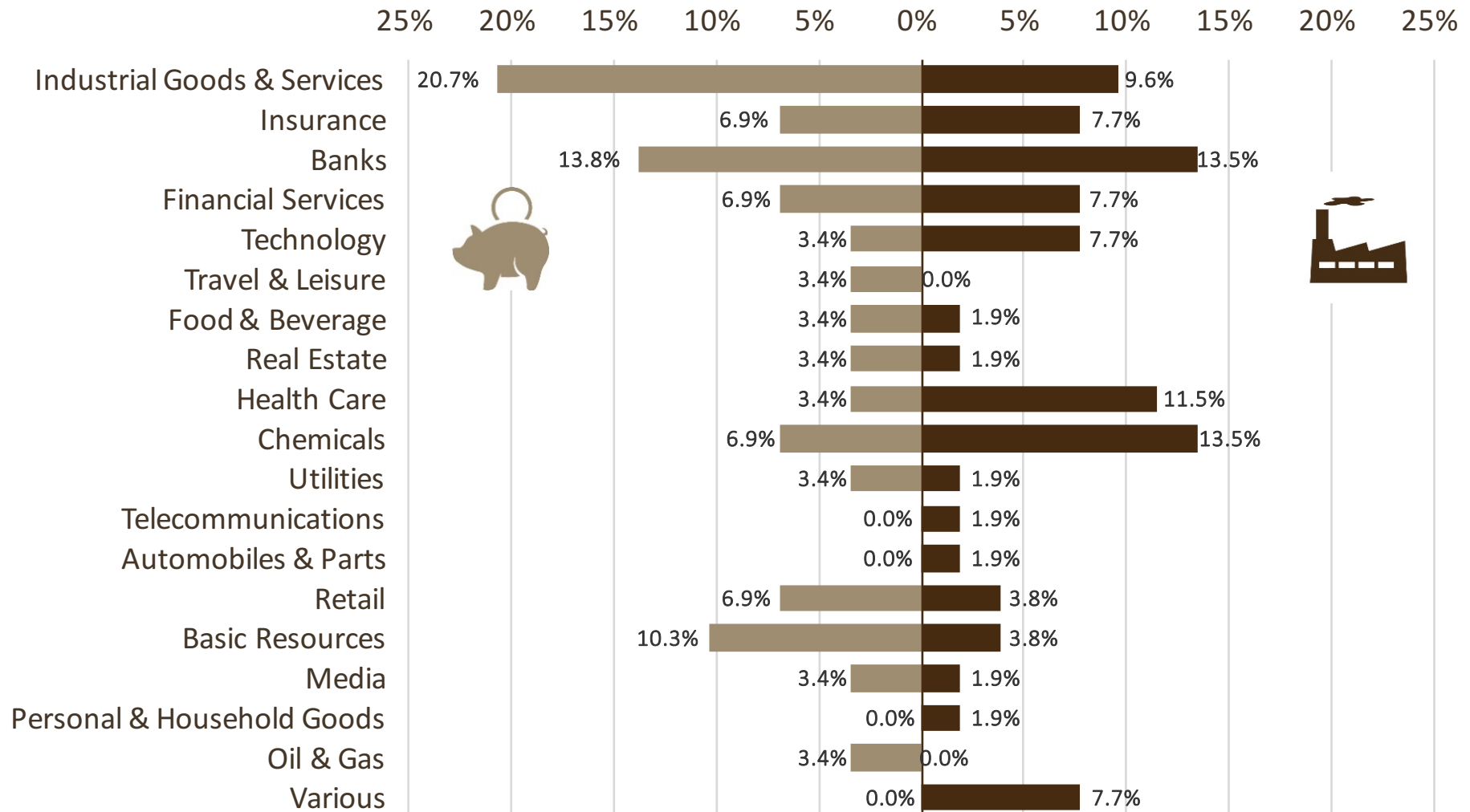


A total of 153 participants filled out the survey  
(+ 41.7% compared to 2014)



# Participating industries

Sample: pension funds and issuers only





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## Key results (I/II)



### ➤ **Agenda items: relevance and effort**

- Items regarding compensation required the greatest effort from both issuers *and* investors, but are not considered as the most important drivers of shareholder value
- For all surveyed groups, the election of board members has the greatest relevance for shareholder value

### ➤ **Disclosure: quality and quantity**

- The surveyed investors are generally not looking for more information, but for more *relevant* information
- Investors and issuers are split on standardizing disclosure



## Key results (II/II)



- **Shareholder voting rights: benefits and costs**
  - In contrast to asset managers, a substantial fraction of pension funds attest little value to voting rights
  - Issuers consider voting rights as a means for shareholders to express an opinion, with only limited influence on a firm's value creation
  
- **Regulation: hopes and fears**
  - Investors and issuers eye future regulatory efforts critically (e.g., regarding prospective voting regimes or compensation caps), and have different views on opting out provisions





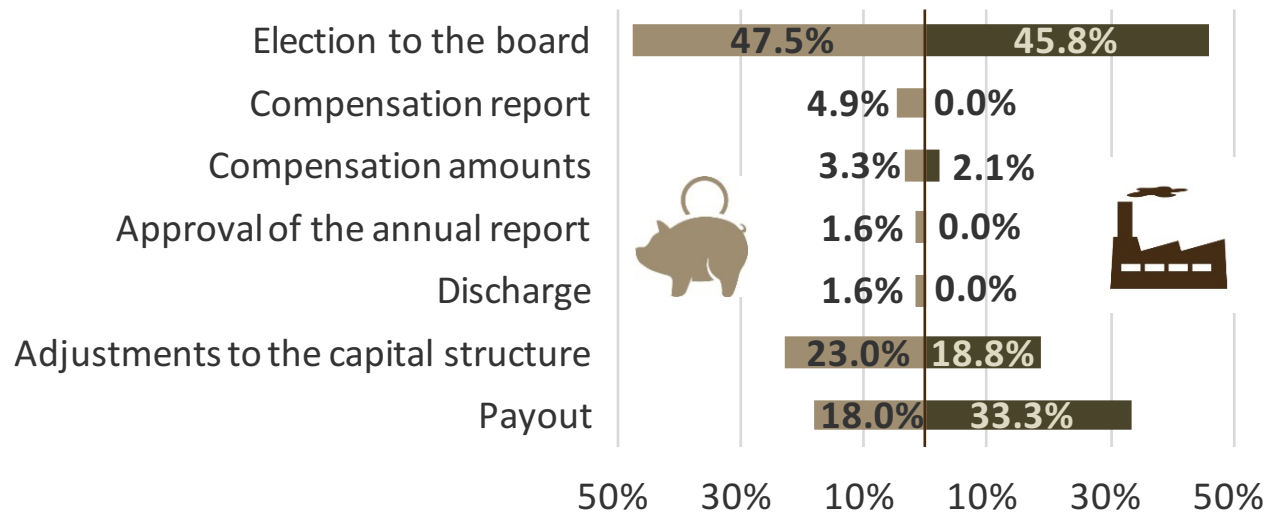
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# Agenda items: relevance

Agenda items with the greatest relevance for a firm's value generation



	Pension funds	CH asset managers	Int. asset managers
Election to board	40.6%	50.0%	63.6%
Comp. report	3.1%	5.6%	9.1%
Comp. amounts	6.3%	0.0%	0.0%
Approval AR	0.0%	5.6%	0.0%
Discharge	0.0%	5.6%	0.0%
Capital structure	28.1%	16.7%	18.2%
Payout	21.9%	16.7%	9.1%

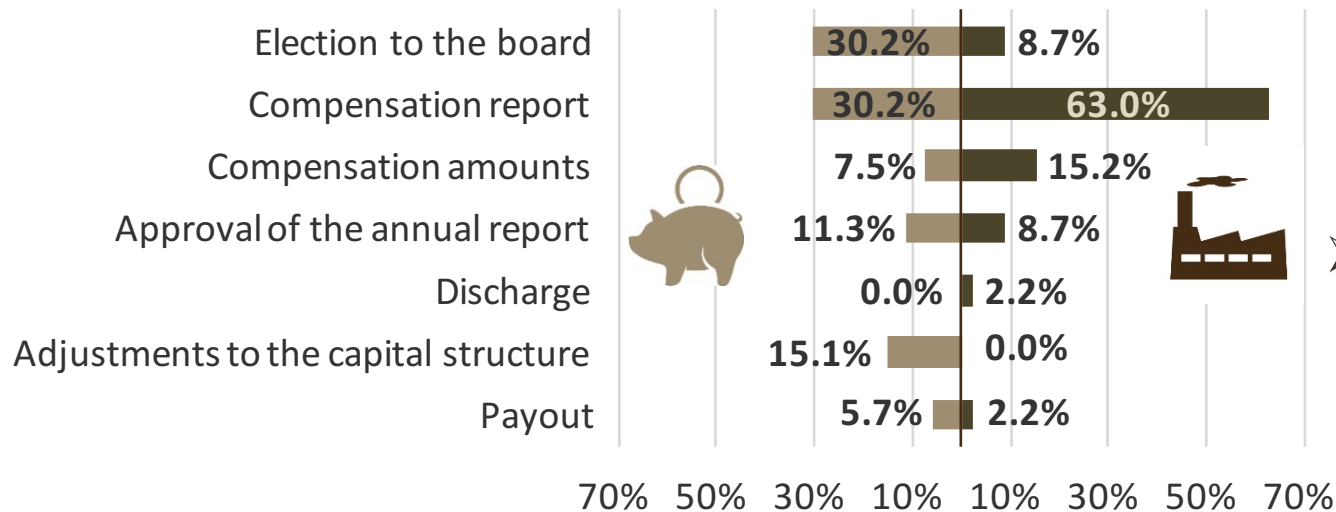
Question: Consider the following agenda items, which are subject to a shareholder vote at Swiss annual general meetings. In your opinion, which vote has the largest impact on the value generation of a company in general?

- Investors and issuers largely agree on the relevance of different agenda items for a firm's value creation
- Board elections are considered the most value-relevant agenda items
- In contrast, agenda items on compensation are of comparably little relevance



# Agenda items: effort

## Agenda items associated with the greatest preparation effort



➤ 38% of the investors and 78% of the issuers dedicated the highest effort to compensation items

➤ For investors, the preparation of board elections is comparable in exerted effort

	Pension funds	CH asset managers	Int. asset managers
Election to board	25.0%	42.1%	20.0%
Comp. report	37.5%	21.1%	30.0%
Comp. amounts	4.2%	5.3%	20.0%
Approval AR	16.7%	10.5%	0.0%
Discharge	0.0%	0.0%	0.0%
Capital structure	12.5%	15.8%	20.0%
Payout	4.2%	5.3%	10.0%

Question: Consider the following agenda items, which are subject to a shareholder vote at Swiss annual general meetings.  
On which agenda item did you spend the most time in preparing the voting decision during the AGM season 2015?

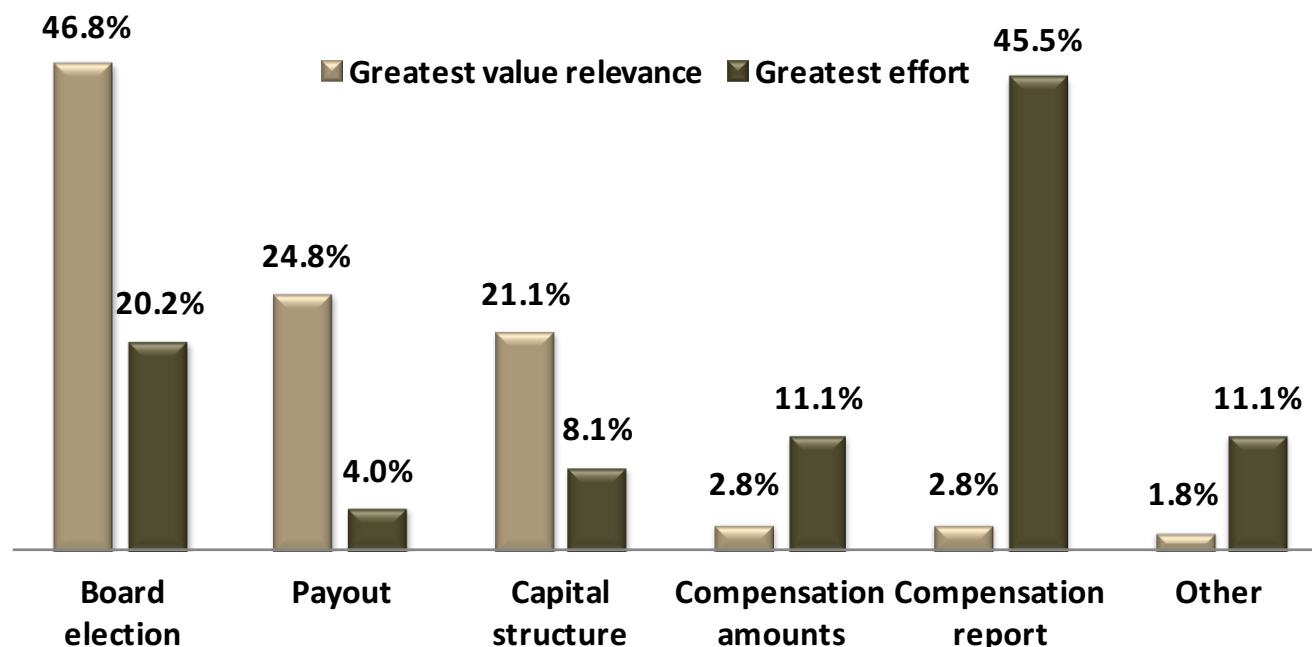


# Agenda items: relevance vs. effort



Comparison of the agenda items' value generation relevance and preparation effort  
Sample: investors and issuers pooled

Issuers and investors were surveyed on the agenda item with the greatest impact on value generation for a company (value relevance; 109 answers) and on the agenda item with the greatest effort requirement during the AGM season 2015 (effort; 99 answers).



- Large discrepancy between greatest effort and greatest perceived value relevance
- Careful interpretation: Question was about most important item (compensation may very well be seen as quite important)

Consider the following agenda items, which are subject to a shareholder vote at Swiss annual general meetings.

Question regarding value generation: In your opinion, which vote has the largest impact on the value generation of a company in general?

Question regarding effort: On which agenda item did you spend the most time in preparing the voting decision during the AGM season 2015?



## Plan for this presentation

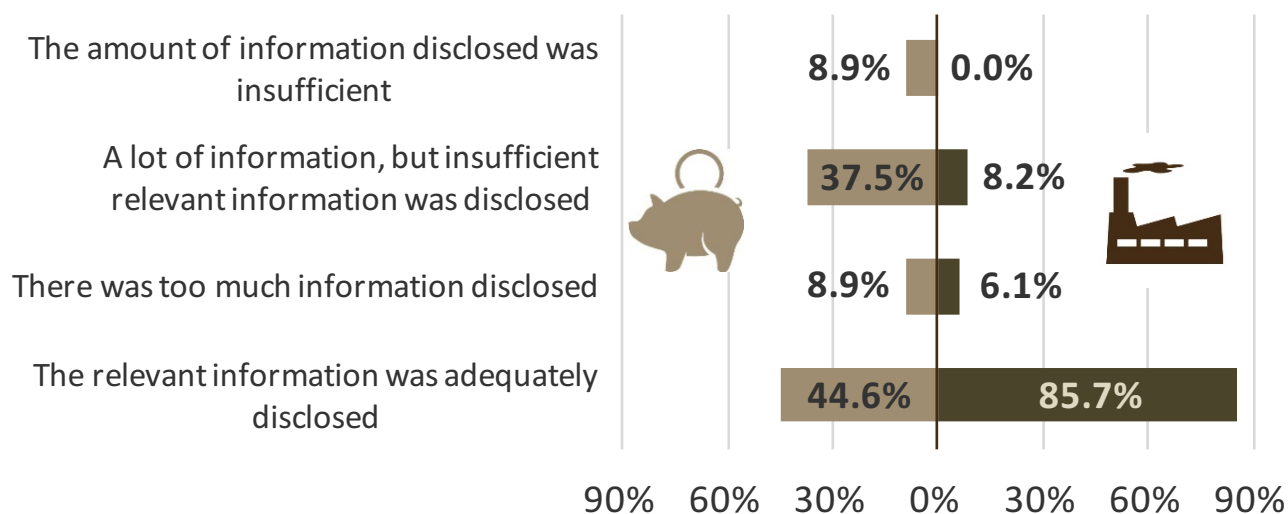
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# Disclosure: quality vs. quantity



## Relevance of disclosed information on compensation in general



- The effort on compensation items may be reduced by orienting disclosure more towards shareholders' needs
- Almost 50% of the investors look for more or more relevant information
- This perception largely remained unchanged compared to last year

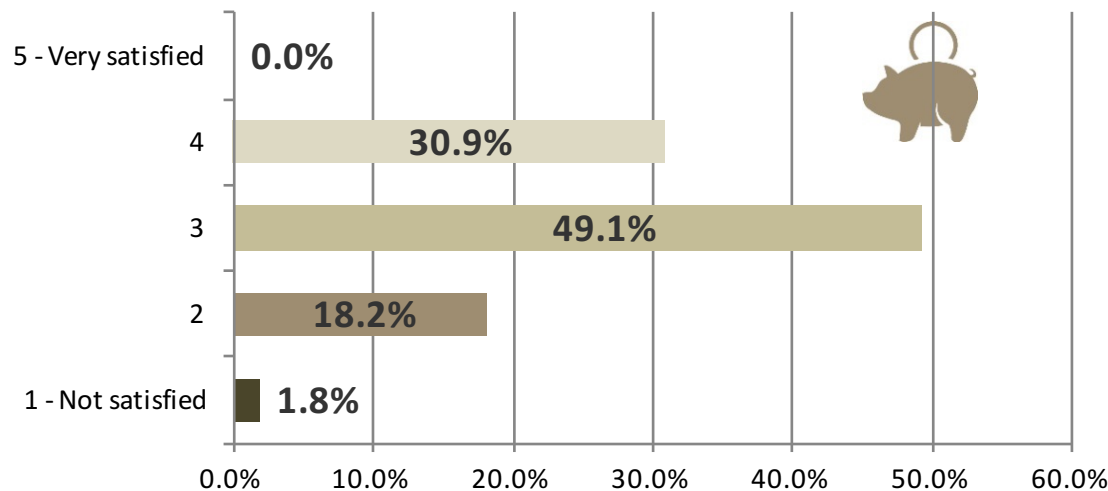
	Pension funds	CH asset managers	Int. asset managers
The amount of information disclosed was insufficient	9.4%	0.0%	25.0%
A lot of information, but insufficient relevant...	37.5%	25.0%	62.5%
There was too much information disclosed	12.5%	6.3%	0.0%
The relevant information was adequately disclosed	40.6%	68.8%	12.5%

Question: Some companies disclose comprehensive details in their compensation report, while other companies stick to the legal minimum requirements. How would you assess the general disclosure quality during the AGM season 2015?



# Disclosure: traceability

**Traceability of proposed compensation amounts**  
**Sample: investors only**



- Less than one third of the investors was actually satisfied with the disclosed information, no one was very satisfied
- Half of the investors are indifferent regarding the importance of the compensation information

	Pension funds	CH asset managers	Int. asset managers
5 - Very satisfied	0.0%	0.0%	0.0%
4	34.5%	43.8%	0.0%
3	55.2%	37.5%	44.4%
2	10.3%	18.8%	44.4%
1 - Not satisfied	0.0%	0.0%	11.1%

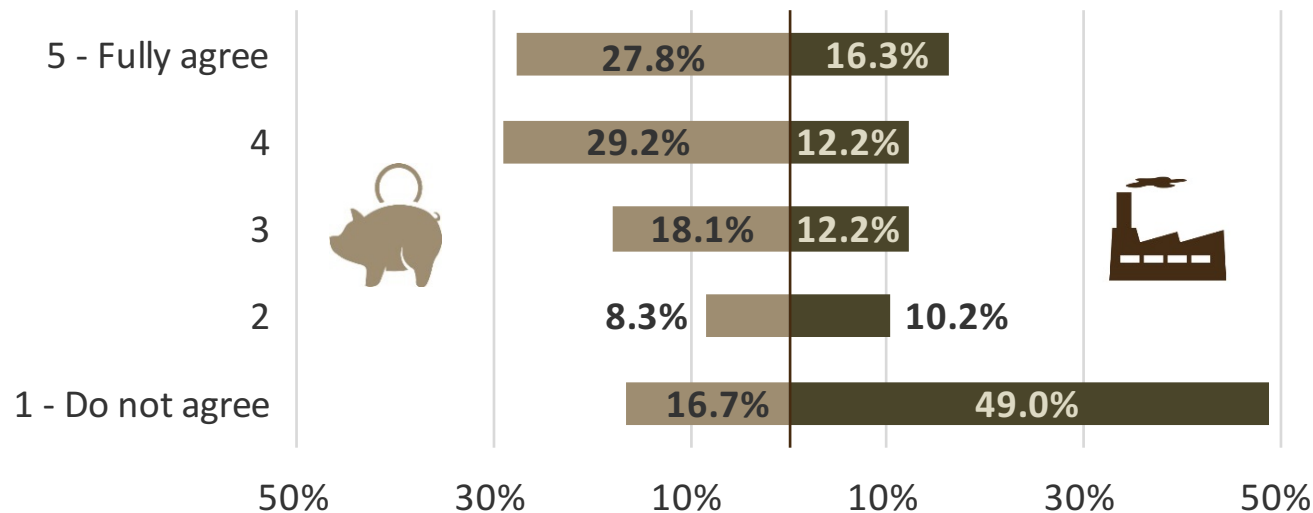
Question: How satisfied were you with the issuers' disclosure with respect to the traceability of the proposed compensation amounts during the AGM season 2015?



# Disclosure: standardization



## Standardization of compensation disclosure



- A standardized disclosure may be seen as facilitating the understanding of compensation systems
- A majority of investors favor a standardized disclosure, half of the issuers disagree

	Pension funds	CH asset managers	Int. asset managers
5 – Fully agree	27.8%	21.7%	38.5%
4	22.2%	34.8%	38.5%
3	16.7%	21.7%	15.4%
2	11.1%	8.7%	0.0%
1 – Do not agree	22.2%	13.0%	7.7%

Question: How do you perceive the following trends in regulation related to corporate governance in Switzerland?  
 Companies should adhere to a standardized reporting format for general disclosure requirements (for example in relation to compensation matters).





## Implications: agenda items & disclosure

- A potential gap (inefficiency) between value relevance and effort exists for various agenda items, most prominently for compensation-related items
- There is, however, convincing evidence regarding the (empirical) relevance of compensation systems for corporate decisions and thus shareholder value
- Standardizing compensation disclosure is not a panacea
- SWIPRA: Providing a more relevant disclosure, in particular on pay-performance, reduces investors' effort and supports value generation internally
- SWIPRA: Board elections should be prepared and documented carefully by issuers



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# Voting rights: benefits vs. costs

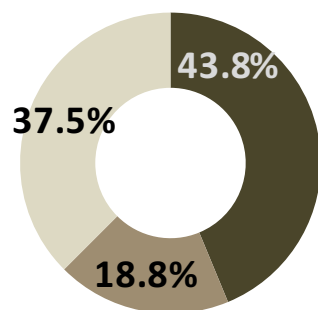


## General value of shareholder voting rights for investors

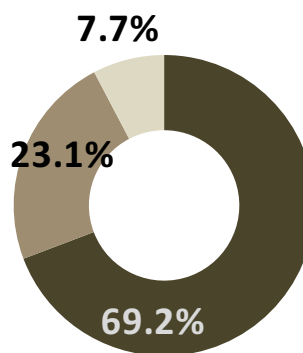
Sample: investors only

- Exercising voting rights may, overall, generate value in the medium term
- Costs and benefits of exercising voting rights are balanced
- Exercising voting rights is unnecessary

### Pension funds



### Asset managers



- Past regulation has considerably increased shareholder power
- Yet, more than one in three pension funds does not assign value to this
- By contrast, more than two thirds of asset and fund managers believe that exercising voting rights can generate value

	CH asset managers	Int. asset managers
Exercising voting rights may, overall, generate value in the medium term	56.3%	90.0%
Costs and benefits of exercising voting rights are balanced	31.3%	10.0%
Exercising voting rights is unnecessary	12.5%	0.0%

Question: In your opinion, what is the general value of shareholder voting rights for your organization?

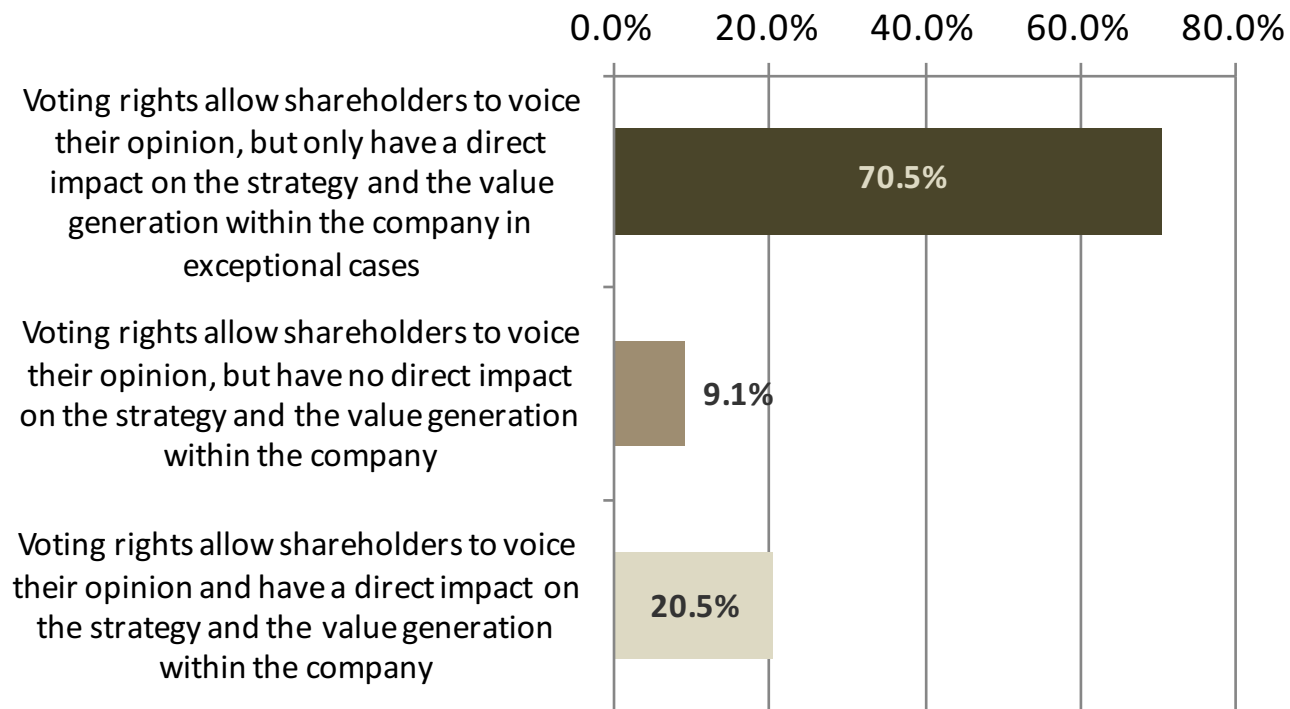


# Voting rights: benefits vs. costs



## General value of shareholder voting rights for issuers

Sample: issuers only



- A majority of issuers interpret shareholder votes as advice / opinions
- Only a minority actually believes that shareholder votes impact a company's value generation

Question: In your opinion, what is the general value of shareholder voting rights for the development of your company?



## Implications: voting rights

- Disagreement regarding the value of shareholder voting rights
  - A substantial fraction of pension funds (a target group of the OaEC!) does not see an added value
  - Issuers see an advisory instead of a direct control function
- Surprising in light of
  - recent developments in Switzerland (e.g. SIKA, LafargeHolcim, etc.)
  - the vast amount of passive equity investments which only leave voting rights as a control measure (no voting by feet)
  - empirical research, which provides evidence that voting rights indeed have a value, particularly in exceptional circumstances
- SWIPRA: Voting rights carry value which should be used in direct and indirect investments



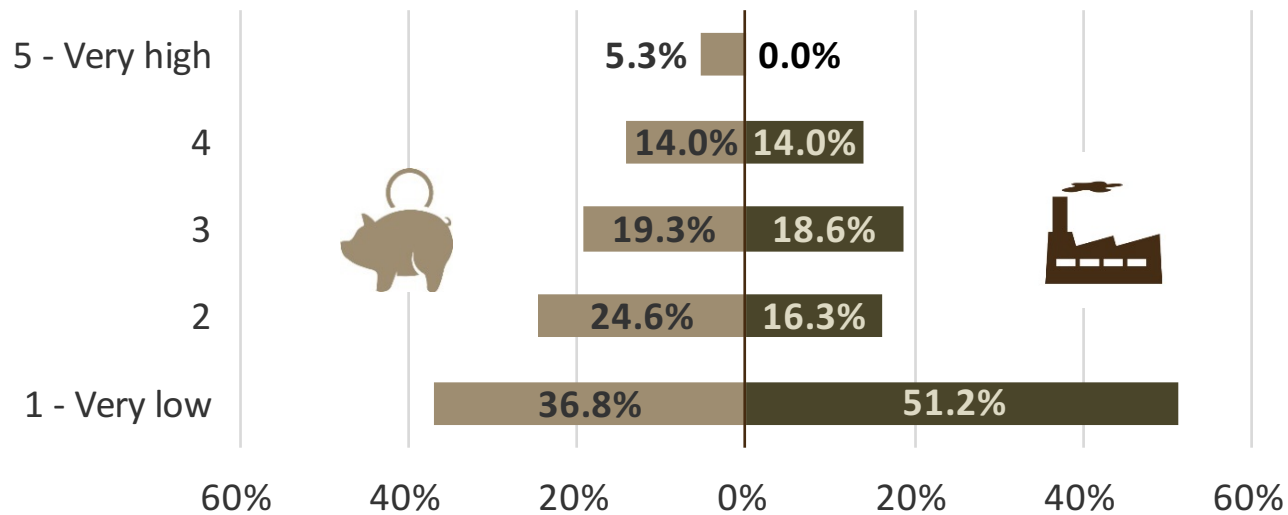
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# Regulation: OaEC impact

## Balance between positive aspects and implementation costs of the OaEC



- The majority of investors and issuers do not expect the OaEC to have a positive net effect
- By contrast, over 40% of international asset managers think that the OaEC's positive effects outweigh the implementation costs
- Concerns in particular regarding pay-for-performance impact (see additional results)

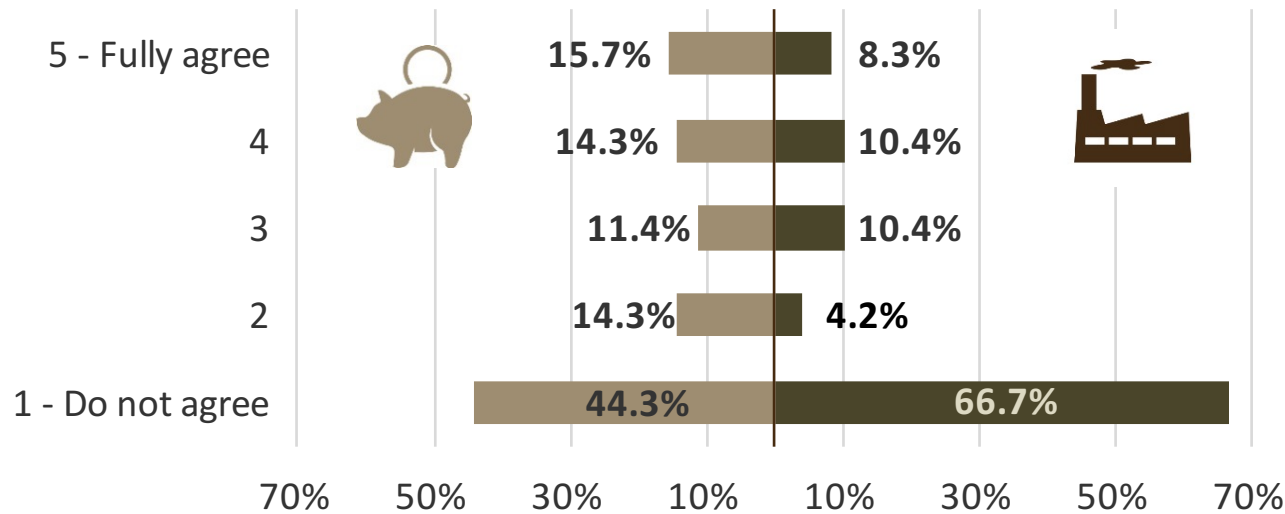
Question: In your opinion, what is the likelihood that the positive aspects of the OaEC outweigh the implementation costs of the OaEC for your organization?



# Regulation: current issues



Only retrospective (ex-post) votes on performance-based compensation should be allowed



- The majority of investors and issuers does not see a need to restrict prospective voting regimes
- 30% of investors, mainly driven by pension funds, think that only retrospective votes should be allowed

	Pension funds	CH asset managers	Int. asset managers
5 – Fully agree	16.7%	17.4%	9.1%
4	16.7%	8.7%	18.2%
3	8.3%	4.3%	36.4%
2	13.9%	21.7%	0.0%
1 – Do not agree	44.4%	47.8%	36.4%

Question: How do you perceive the following trends in regulation related to corporate governance in Switzerland?  
 Votes on compensation amounts should be further regulated to allow only retrospective (ex-post) votes on performance-based compensation.

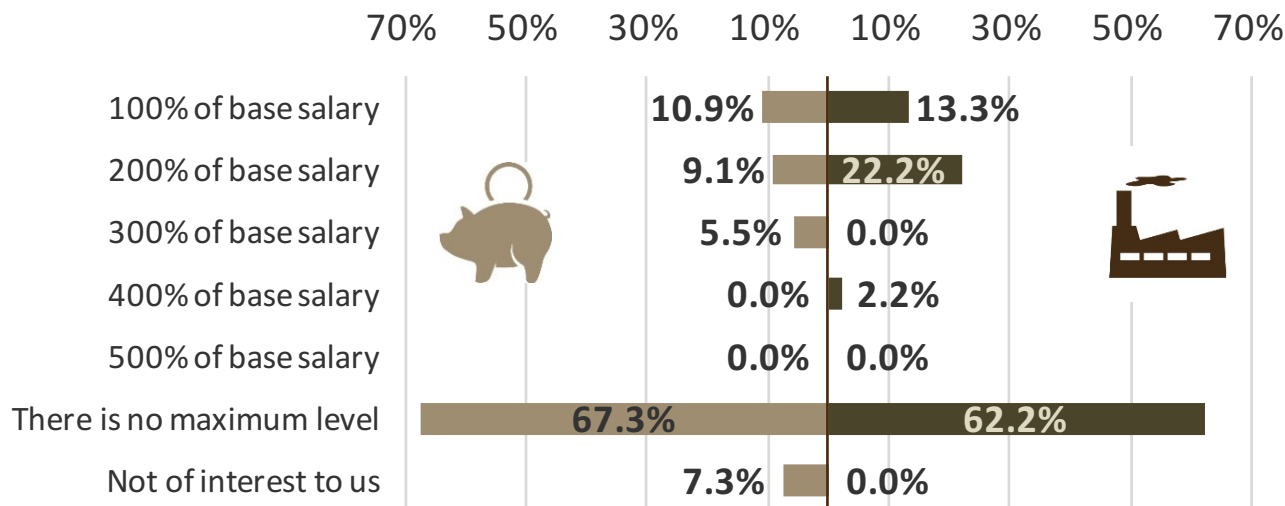




# Regulation: current issues



## Cap on individual cash-bonus payments



- The vast majority of investors and issuers is against caps on cash-bonus payments
- However, all participants share the opinion that cash-bonus payments need to be linked to the company's performance

	Pension funds	CH asset managers	Int. asset managers
Not of interest to us	6.5%	11.8%	0.0%
There is no maximum level	61.3%	76.5%	71.4%
500% of base	0.0%	0.0%	0.0%
400% of base	0.0%	0.0%	0.0%
300% of base	9.7%	0.0%	0.0%
200% of base	12.9%	5.9%	0.0%
100% of base	9.7%	5.9%	28.6%

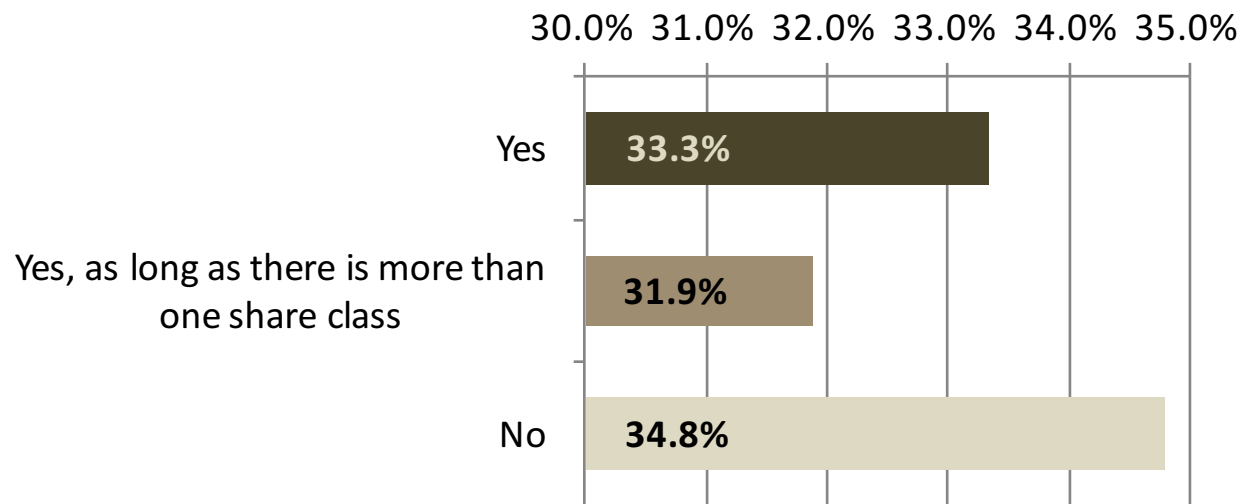
Question: In your opinion, what should be the maximum for individual cash-bonus payments?



# Regulation: current issues



„Opting-out“-provisions  
Sample: investors only



- The majority of investors (65.2%) supports a cancellation of opting-out provisions for companies with a dual-class share structure
- A substantial part of investors, especially international asset and fund managers (76.9%), supports a general abolishment

	Pension funds	CH asset managers	Int. asset managers
Yes	26.5%	18.2%	76.9%
Yes, as long as there is more than one share class	35.3%	40.9%	7.7%
No	38.2%	40.9%	15.4%

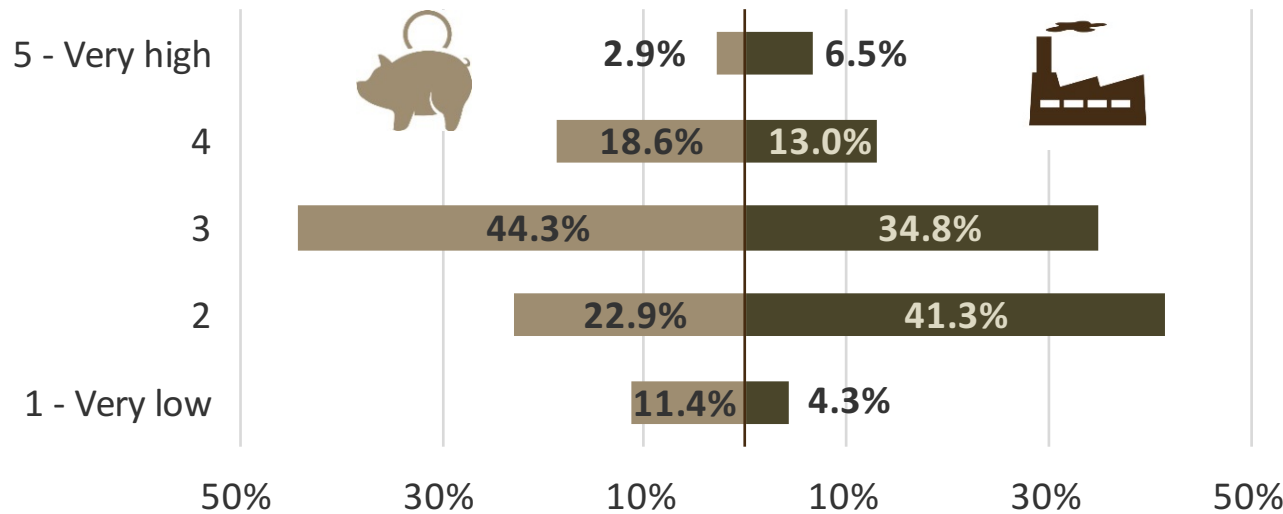
Question: „Opting-out“-provisions (an acquirer of a large block of shares (e.g., 33 1/3% of the shares outstanding) is not obliged to provide a purchase offer with similar terms to all shareholders) should be prohibited.



# Regulation: hopes and fears



## Congruence between future regulation and own preferences



- Only one fifth of all surveyed participants expect future regulation to be in their interest
- Issuers are generally more pessimistic than investors regarding the effects of further regulation

	Pension funds	CH asset managers	Int. asset managers
5 – Very high	2.9%	4.3%	0.0%
4	8.6%	26.1%	33.3%
3	54.3%	34.8%	33.3%
2	22.9%	21.7%	25.0%
1 – Very low	11.4%	13.0%	8.3%

Question: Consider again the previously raised regulation topics. In your opinion, what is the probability that your overall preferences with regards to an increase / decrease in regulation will be realized?



## Implications: regulation

- Investors and issuers generally have a clear view on several currently discussed legal and regulatory developments:
  - Prospective voting regimes should not be restricted
  - Bonus caps should not be made mandatory
  - Opting-out provisions should be abolished from the investors' point of view; this contrasts with the issuers' opinion
- A majority of the participants believes that overall the OaEC induced more costs than provided benefits, and they worry about costs and benefits of future laws and regulations
- SWIPRA believes that regulation and legal developments should also be guided by economic considerations, weighing benefits and costs for different types of companies



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## Summary and outlook

- This survey presents a unique view on the opinions of both institutional investors and issuers
- Recent corporate governance rules and regulations have arguably led to some inefficiencies (relevance-effort gap)
- Market participants want lawmakers and regulators to tread carefully when considering further extensions of regulation
- For market discipline to work, it is crucial that shareholders make use of the rights they already have



# Contact

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