

Why the Shareholder Rights Directive II (SRD II) matters?



Pitfalls of non-compliance



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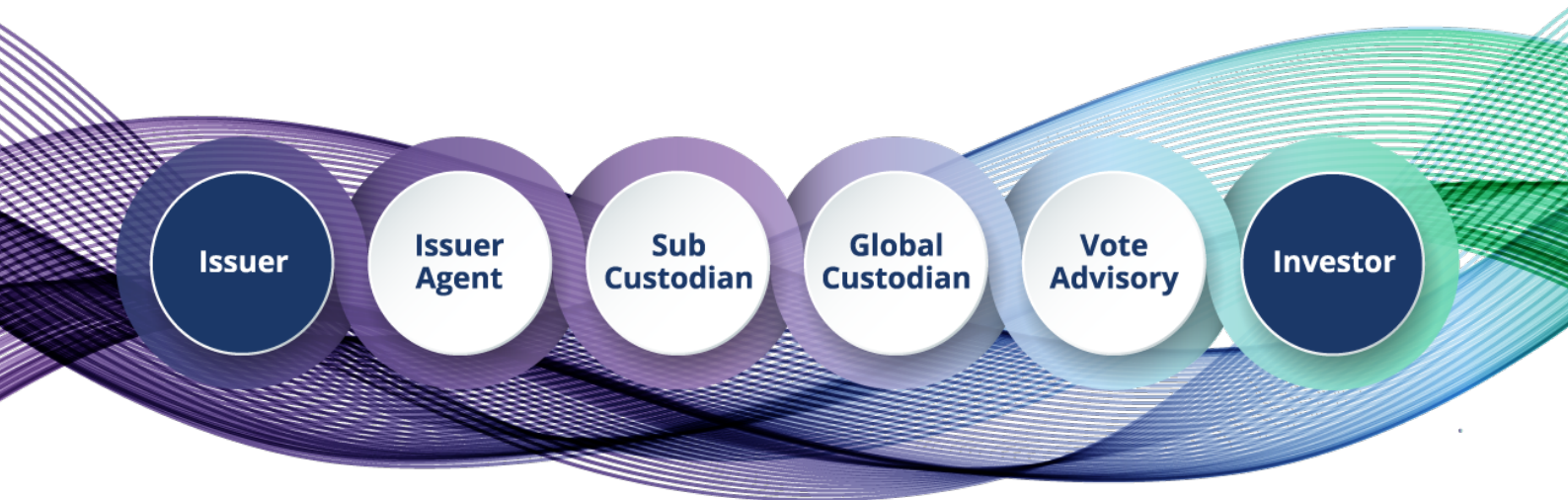
Pitfalls of non-compliance

Executive Summary

With SRD II regulations now firmly established in most European Countries, intermediaries potentially face severe penalties for breaching Shareholder Identification rules under SRD II.

However, with good planning and the right partners, not only can penalties be completely avoided, but intermediaries may improve their levels of client service through strong compliance.

Find out more about avoiding pitfalls in individual geographies across Europe, and how you can stay compliant, in this White Paper brought to you by Proxymity supported by data from international law firm, Clifford Chance LLP.



Introduction

In this white paper we will explore the impact of shareholder identification under the Shareholder Rights Directive II (SRD II), which came into effect on 3, September 2020, on you, the intermediary.

SRD II brings extra obligations to both issuers and all intermediaries in the investment chain. While issuers have the added responsibility of announcing meetings and voting, the greatest weight of responsibility lies with you, the intermediaries, in managing shareholder identification.

It is, you, the intermediary, who is tasked with both disclosing shareholder information and passing requests through the chain of custody. It is also your responsibility to ensure that the process is carried out in a transparent and efficient manner, with a set of policies in place, that conform to SRD II regulations.

We'll look at the limit and scope of the new instruction for intermediaries, analysing what it covers, who it covers and how it impacts organisations. Most importantly, we'll clearly outline your obligations under the new directive and reveal the penalties that your organisation could incur for failing to comply with SRD II.

Shareholder Rights Directive II (SRD II) – what is it?

For issuers to engage shareholders, first it must be able to identify them.

If you are an intermediary reading this paper, the main sea-change is that you are now required to provide information relating to the identity of your shareholders. You also have an obligation to pass the request on until the shareholder is identified.

Who does it apply to?

If you are an intermediary that services clients holding EEA issued securities, then SRD II applies to you.

However, the issue of who is and who isn't affected by SRD II is much more complex and nuanced than that.

There are “added complexities” for “third country intermediaries” who operate outside of the EU, and it is possible that their local data privacy laws could come into conflict with SRD II.

Take a Japan-based intermediary for instance. The intermediary may not have a registered office in the European Union, so you may think that it would not be subject to SRD II regulation. However, SRD II has global reach. If the intermediary holds shares in an EEA-based issuer and it is traded on a regulated exchange, then it is actually subject to SRD II. i

It is not only important, therefore, to have an in-depth understanding of both the local laws and your SRD II obligations. You must also have developed a set of robust policies which enables you to meet SRD II requirements, while not falling foul of local data privacy laws.

Nigel Little, who has worked for the BNY Mellon, Deutsche Bank and Euroclear, before joining Proximity, explains the scope of an intermediary's SRD II responsibilities:



The directive, applies to **companies listed on regulated exchanges in EEA countries**, i.e. the 27 nations of the European Union and Iceland, Liechtenstein and Norway

“It’s vitally important that intermediaries are aware of shareholder identification and the obligations placed upon them by SRD II, in addition to the local data privacy rules to which they must conform.

Intermediaries must respond to disclosure requests without delay and via a secure, machine-readable communication channel, while forwarding on to the next intermediary in the custody chain until the underlying shareholder is identified.

While it may be considered an unnecessary burden for intermediaries with intangible benefits, **shareholder identification provides great value to issuers and investors by enabling them to connect.**”


Nigel Little, Product Manager, **Proximity**

“We also see an increase in the usage of Shareholder ID data, some issuer agents are performing shareholder ID in parallel with the general meeting and rejecting votes when the vote received at the beneficial owner level does not reconcile with that of the disclosure.”


Therefore, **intermediaries not disclosing their investor clients also carry the risk that their votes not being counted.**”

“Other markets are exploring, or in some instances, are already starting to use Shareholder ID in parallel with cash dividends and **only paying those investors who have disclosed.** This is creating reconciliation problems for intermediaries who are receiving partial payment, and without access to the shareholder id data are unable to pay their clients.

Consequently, **intermediaries not disclosing their investor clients risk their clients not being paid**”.



SRD II seeks to **enhance shareholder engagement, transparency, and accountability.**



“SRD II penalties are not purely financial but also potentially **client impacting.**”

Jonathan Smalley – COO, Proxymity



ACCOUNTS RECEIVABLE
GRUBER LAW OFFICES
ONE CALL...
THAT'S ALL!

Compliance Issues

Lack of **clarity**

Added compliance **burden**

Consequences for non-compliance

SRD II challenges

Lack of clarity

While much of the SRD II regulation is clear, some of it remains open to interpretation. The scope of SRD II covers listed companies with a registered office in a member state and admitted to trading on a regulated market. However, in some markets the law has been extended to include other securities. Meanwhile in other markets, the ISO20022 introduced for SRD II messages are being used for local registration purposes for non-SRD II securities.

The directive is also a little vague requires that as an intermediary, you are required to communicate using machine readable text, which conforms to the ISO 20022 standards. Some high-tech investor platforms have been configured to automatically ensure that you are ISO 20022 compliant. ii

Added compliance burden

These complexities around SRD II place an increased burden of responsibility on the shoulders of you, the intermediary. Under the new legislation, you must fulfil all the duties laid out in the new directive, which has increased your workload. There are also new data protection challenges to consider as you could be transmitting confidential PII data which has strict GDPR guidelines to consider.

Penalties for non-compliance

Intermediaries who fail to comply with SRD II face tough penalties. So, what is the fine for breaching SRD II?

There is no simple answer as the 'Measures and Penalties' section of the directive states that independent EU states set their own enforcement policies. So, in theory, each of the nations who have also signed up to the directive have the power to issue separate fines. To complicate matters further, there are different fines for different breaches.

Below, is a chart ⁱⁱⁱ documenting the fines which can be imposed in the United Kingdom and the European Union's ten largest economies as ranked by Statista and using public data sourced from Clifford Chance LLP. ^{iv}

Potential fines by Country

“SRD II Jurisdictional survey summary table”

More detailed information available from our source published by Clifford Chance LLP: <https://www.cliffordchance.com/home.html>

Germany



Power to fine intermediaries up to **€500,000**

Austria



Power to fine intermediaries **up to €25,000 for each offence**

France



Fines up to **10 percent of the previous year's turnover**. ACPR licensed intermediaries may be subject to other regulatory action, including **licence withdrawal**

Italy



Administrative fines range from **€30,000 to €150,000**

Spain



Enforcement agencies can issue fines of **up to €5m**. Intermediaries can levy a fine of **up to five times the gross profit received as a result of the benefit**, or 5% of the offender's own funds

Netherlands



Maximum fine for a breaching SRD II is **€830,000**, or 10% of the legal turnover for the legal entity

Poland



Intermediaries can be hit with a fine of **up to PLN500,000 (€108,869.63)** for breaching SRD II

Sweden



Fines should not exceed **two times the profit received**, or **10% of the turnover in previous year**. A fixed fine can also be issued, while other sanctions can be imposed

Belgium



Fines have not been written into the legislation

Ireland



In the Republic of Ireland, a category C offence is punishable with a fine of **€5,000 and/or 6 months in prison**

Proximity

More detailed information available from our source published by Clifford Chance LLP: <https://www.cliffordchance.com/home.html>

The Solution – technology

With intermediaries needing to respond to disclosure requests and send them onward to clients effectively, the antiquated methods of communication that has been relied on for years, are fast being replaced by leading-edge technology.

The question is, if you are an intermediary, how do you navigate the myriad of market nuances, but still notify intermediary clients promptly and securely while meeting the tight response deadlines imposed by the new directive?

Andrew Myers, Head of Product at Proximity, explains, “there are three widely known solutions available to intermediaries to handle disclosure requests.”

1. Build an in-house IT solution,
2. Buy an off the shelf solution from an IT vendor,
3. Employ a third-party service provider to manage the service.

In-house solutions typically have heavy implementation and ongoing maintenance costs. A skilled and disciplined operations/compliance team must be employed operate the solution and mitigate the risk of a confidential data breach. Vendor solutions and managed services have lighter implementation costs, plus they take away burden of any future development costs. The vendor solution still needs you to employ an operations/compliance team, whereas the benefit of the managed service is all aspects are outsourced to the provider including the market expertise, however there are the management costs to consider.

One further unexpected consideration is the extraordinarily high number of disclosure requests received directly from Solicitation and Market Intelligence companies who are leveraging the directive to flood the markets with direct disclosure requests at intermediary level. Each of these require thorough investigation by the recipient as “First Intermediary” to prevent a data security breach. Does the agent have authority to act on behalf of the issuer? Does the agent have sufficient data security measures in place and in accordance with GDPR? Is the issuer eligible to request disclosure under the SRD II directive?

“Each option brings its own merits, and any decision should be based on the **market and legal expertise within the organisation, the volume of European securities held and the location of the intermediary in the custodial chain.**”

Andrew Myers – Head of Product,
Proximity



How Proxymity can help – our solutions

Choosing the right partner is key, Proxymity can help you with both the second and third options mentioned above, providing flexibility and choice.

Proxymity digitally connects the world's ecosystem of issuers, intermediaries, and investors in real-time, bringing unprecedented transparency, efficiency, and accuracy to traditional paper processes.

Trusted by the world's largest financial institutions, including seven of the top-ten global custodians, who represent over US\$200 trillion in assets under custody, it is the leading digital investor communications platform, serving over 25 markets worldwide, delivering a continuous "golden source" reconciled record throughout.

Proxymity's mission is to operate for the benefit of the whole ecosystem, not just one part of it, to help deliver its mission, Proxymity offers two products to assist intermediaries with their disclosure requests.

Shareholder ID

A fully managed service with the intermediary connected to the platform, **all disclosure requests are routed to Proxymity** for Proxymity to authenticate and act upon with **real time compliance monitoring and reporting**.



Shareholder ID Access

A partially managed service, **all disclosure requests are routed to Proxymity** for Proxymity to authenticate, intermediaries provide the required holder information through the Proxymity platform dashboard, for Proxymity to act upon with compliance monitoring and reporting.



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financial institutions,
Proxymity's mission is to
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Summary

While the new directive will promote greater governance and transparency, SRD II places an added burden of responsibility on you, the intermediary.

For intermediaries to enable you to fulfil your and your client's obligations, ensure you have understood each market for which you operate and have a solution in place to react to authentic Shareholder ID requests promptly and securely, monitoring and reporting the results for SRD II compliance.

Indeed, if SRD II is the driver for better corporate governance, then as we step into a new age of greater transparency, technology, which ensures the fast, transparent and accurate transfer of information, is the enabler. It is something that the industry should wholeheartedly embrace.



End Notes and Source information

ⁱ Bobsguide

Ten things you need to know about the Shareholder Rights Directive II

<https://www.bobsguide.com/articles/ten-things-you-need-to-know-about-the-shareholder-rights-directive-ii/>

ⁱⁱ Bobsguide

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ⁱⁱⁱ Clifford Chance LLP

AFME and AGC – SRD II Jurisdictional survey summary table

^{iv} Statista

Gross Domestic Product at current market prices of selected European Countries in 2021

<https://www.statista.com/statistics/685925/gdp-of-european-countries/>

Contact us

Proxymity connects the world's ecosystem of issuers, intermediaries, and investors digitally in real time, bringing unprecedented transparency, efficiency, and accuracy to traditional paper-based processes. Trusted by the world's largest financial institutions, it is the leading digital investor communications platform, serving over 25 markets world-wide.

Our solutions give public companies confidence that their AGM/EGM agendas are transmitted as "golden source" and provide institutional investors with the time they need to research and vote on corporate decisions, as well as actual digital confirmation that their votes have been received. The digital-native platform, built on highly scalable technology, provides full compliance with the latest regulations such as the Shareholder Rights Directive (SRD II).

Proxymity promotes enhanced environmental, social, and corporate governance (ESG) by improving communication between issuers and investors and making it easier for intermediaries to be efficient, timely and compliant when servicing their clients.

The company is backed by a global consortium of the industry's most influential financial institutions (BNP Paribas, BNY Mellon, Citi, Computershare, Deutsche Bank, Deutsche Börse, HSBC, J.P. Morgan, Mediant, State Street).

For more information, visit <https://proxymity.io/>