Position Paper

Insurance Europe's comments to the European Commission's proposal to revise the Shareholder's Rights Directive

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Insurance Europe would like to take the opportunity to share its key messages and comments on the Commission's proposal on the review of the Shareholder's Rights Directive. Insurance Europe understands that this proposal is part of the long-term financing discussion launched by the European Commission back in 2012/2013, which it welcomed.

Insurance Europe's comments are mainly focused **on Article 3f, Article 3g and Article 3h**, which it believes deserve careful consideration, to correctly reflect institutional investors' approach to asset and asset/liability management.

Insurance Europe would also like to highlight a number of concerns emerging from **Article 9** of the proposal, regarding related party transactions and remuneration policy.

General comments regarding insurers' role as largest European institutional investors

The insurance industry is the largest European institutional investor, with €8 500bn of assets under management at the end of 2013[1]. Insurers' significant role as investors is a consequence of their primary role of providing protection from risks, as well as long-term savings and retirement products. As most of their liabilities are long-term, investing with a long-horizon perspective becomes a natural match between insurers' assets and their liabilities.

The main driver of insurers' investment decisions is the profile of their liabilities. Insurers' ability to buy long-term and illiquid assets or to withstand market volatility significantly depends on the insurance product and the liabilities those assets back. For example, in the case of unit-linked products, it is policyholders who have the choice over the asset allocation and investment risk, and so withstand market volatility themselves. In the case of fully guaranteed annuity-type products, it is the insurer who designs the product features and the asset allocation in a way that optimises return while securing the pay-off promise made to policyholders.

Insurers' asset allocation is, therefore, highly dependent on the profile of their liabilities and the percentage share of various assets. This can vary significantly from company to company, depending on the business they

[1] Insurance Europe data

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undertake. Insurers' average allocation to equity is 15% and the average allocation to bonds (both corporate and government) is around 60%[2]. European insurers hold around 18% of the total European public equity[3].

Comments on provisions included in the proposed Directive

The proposal targets the equity holdings and investment strategies of life insurance companies (as indicated in Article 1(f)). Insurance Europe believes that, while the Commission's intention to foster long-term financing of the economy via equity investments is understandable, a number of provisions in the proposal appear to be based on flawed and/or misleading assumptions.

Insurance Europe is concerned by the statements reproaching institutional investors that they do not "sufficiently focus" on the long-term performance of their asset holdings and that they do not engage with the companies in which they hold shares. Such a generalisation cannot be made for insurers, and, therefore, it believes that such a view reflects a flawed understanding of how and why insurers invest and should be amended in the final text.

Article 3f (Engagement Policy)

Insurance Europe welcomes the "comply or explain" characteristic of the engagement policy.

However, the notion of "engagement policy", as defined trough the six criteria in Article 3 (f) (1) (a-f), remains too arbitrary, and is not sufficiently clear to be fully understandable. Different institutional investors will have different needs and considerations when deciding what part engagement plays in their investment strategy. It is therefore very difficult and inappropriate for policymakers to determine specifically what the engagement policy by insurers (as investors) should be. Also, it must be reminded that insurers' shares in listed companies, held either directly or through asset managers, are mostly minority stakes and, even in the case of large listed companies, do not exceed a few percentage points.

Insurance Europe remains concerned by the requirement to disclose the implementation and results of the engagement policy "for each company in which insurers hold shares" on an annual basis. Insurance Europe believes that the disclosure requirements can generate significant operational effort and also raises confidentiality concerns. Insurance Europe welcomes the "comply or explain" characteristic of the engagement policy. Insurance Europe is also concerned by the requirement to disclose the implementation and results of the engagement policy "for each company in which insurers hold shares" on an annual basis. Insurance Europe believes that the disclosure requirements can generate significant operational effort and also raises confidentiality concerns.

The insurance industry holds about 18% of the entire equity market across Europe and insurers will, therefore, often hold shares in a large number of companies. While Insurance Europe supports the principle of reporting on the implementation of the engagement policy, it believes that the approach to public disclosure should be carefully considered as there are potential unintended consequences. For example, engagement could be ongoing with a particular company and it could be sensitive to disclose continuing disagreement between a company and its investors. At the extreme, public disclosure of a disagreement between a company and their shareholders could impact shareholder value.

Consequently Insurance Europe is concerned by confidential or commercially sensitive information being

[2] Based on end-2011 Insurance Europe data
[3] Insurance Europe and Oliver Wyman study "Funding the future"

required to be publically disclosed. It is, therefore, essential that the investor is given sufficient flexibility to withhold disclosure if this is commercially sensitive.

- **Article 3g (Investment strategy of institutional investors and arrangements with asset managers)**

Insurance Europe would like to point out that a number of provisions do not accurately reflect how insurers invest.

The investment strategy is about disclosure between the institutional investor and the asset manager. Insurance Europe does not understand what the public interest is in such a disclosure. What is more important is the disclosure between the institutional investor and the asset manager on these issues ahead of the mandate being signed so all parties know and agree on what approach will be taken by the asset manager. There is little value added from public disclosure.

For example, **Article 3g (1)** calls for institutional investors to disclose to the public how their equity investment strategy is aligned with the profile and duration of their liabilities. While institutional investors buy fixed income/cash-flow generating assets to match the cash flows and/or the duration of their liabilities, equity assets are often bought to provide additional return. While in practice equities may be held for longer periods by insurers than certain other investors, they do not have duration targets per se, because they are not backing liabilities with specific cash-flow profiles. Such equities will be traded or held depending on what provides the best long-term performance and will be influenced by both expectations of the under or over performance of particular shares and also of the market as a whole. The Commission proposal appears to be based on the assumption that with long-term products the equity investments must, by definition, be held long-term; while this is true for bonds used for liabilities' matching, it is not true for equity investments. **This reporting requirement should, therefore, be deleted.**

The requirement in article **3g (2) (a),** that each asset manager should be incentivised to align investment strategy with profile and duration of liabilities, is also misleading. As explained above, as part of overall strategic portfolio view, an institutional investor may want to use an asset manager with a short-term investment if that contributes to an enhanced portfolio performance. The institutional investors will themselves assess the asset liability matching at a total portfolio level. **This requirement should, therefore, be deleted.**

- **Article 3h (Transparency of asset managers)**

Insurance Europe underlines that asset managers already report to institutional investors on how they manage the assets under mandate and there is, consequently, no clear benefit of any additional requirements in this respect. In addition, the requirement for asset managers to disclose information to other investors regarding portfolio composition and changes raises significant confidentiality concerns and should be reflected in the final text of the Directive.

- **Article 9 (Related party transactions and remuneration policy)**

Countries which already have these protections for shareholders, such as the UK, are supportive of the Commission's proposals. In particular, the consistent rights and disclosures given to European Shareholders who invest cross-border within the EU should help to increase the attractiveness of and confidence in European stock markets. However, other jurisdictions such as those with a two-tier system are concerned because, as currently drafted, the provisions appear to ignore existing arrangements in countries with a two-tier law system, such as Germany, Austria and France. The role of the supervisory body, which is mandatory in these

countries according to national company law and whose tasks are defined by law, risks being minimised by the European provisions. For example, in such countries, it's the supervisory board that takes decisions regarding the remuneration policy, and not the shareholders. In addition, the requirements on related party transactions must not undermine the role of managing bodies in Member States where a two tier system exists. Therefore, the final provisions need to allow for an appropriate interaction between the EU directive and local company law in all member states.

Insurance Europe is the European insurance and reinsurance federation. Through its 34 member bodies — the national insurance associations — Insurance Europe represents all types of insurance and reinsurance undertakings, eg pan-European companies, monoliners, mutuals and SMEs. Insurance Europe, which is based in Brussels, represents undertakings that account for around 95% of total European premium income. Insurance makes a major contribution to Europe's economic growth and development. European insurers generate premium income of more than €1 110bn, employ almost one million people and invest over €8 500bn in the economy.