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Say on Pay Around the World

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SAY ON PAY AROUND THE WORLD

RANDALL S. THOMAS*
CHRISTOPH VAN DER ELST**

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INTRODUCTION

Shareholders have long complained that top executives are overpaid by corporate boards irrespective of their performance.[1] Traditionally largely powerless to prevent these perceived abuses, investors have sought a way to gain greater influence over directors' compensation decisions. While many governments responded by increasing the level of corporate disclosures on compensation packages and policies, and occasionally tinkering with tax policies in efforts to reduce pay levels, none of these changes has had much impact.[2]

However, investors have continued to put pressure on governments to change the status quo. In 2002, these efforts led the U.K. to adopt legislation requiring public companies to permit their shareholders to have a mandatory, nonbinding vote on the compensation of their top executives ("Say on Pay").[3] Since that time, there has been a wave of Say on Pay legislation enacted in countries around the world, including the U.S., Australia, Belgium, the Netherlands, and Sweden, with Swiss voters most recently approving a binding shareholder vote on executive remuneration.[4] In this Article, we examine these new legislative iniatives carefully and ask why they have been so widely adopted, how effective they are, and whether they are likely to be adopted in other countries.[5]

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1. Examples of these complaints are mentioned throughout LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION (2004). For a conflicting view, see John E. Core, Wayne R. Guay & Randall S. Thomas, *Is U.S. CEO Compensation Inefficient Pay Without Performance?*, 103 MICH. L. REV. 1142 (2005).

2. In fact, some commentators claim that these regulatory initiatives have generally been ineffective or counterproductive. Kevin J. Murphy, *The Politics of Pay: A Legislative History of Executive Compensation*, *in* RESEARCH HANDBOOK ON EXECUTIVE PAY 11, 11 (Randall S. Thomas & Jennifer G. Hill eds., 2012).

3. Fabrizio Ferri & David A. Maber, *Say on Pay Votes and CEO Compensation: Evidence from the U.K.*, 17 REV. OF FIN. 527 (2013). For an early article debating the merits of Say on Pay that preceded the U.K. adoption, see Brian R. Cheffins & Randall S. Thomas, *Should Shareholders Have a Greater Say over Executive Pay?: Learning from the U.S. Experience*, 1 J. CORP. L. STUD. 277 (2001).

4. The Swiss Parliament enacted the law on November 20, 2013, which came into force on January 1, 2014 but contains a long transition term. Press Release, Der Bundesrat, Eidgenössisches Justiz- und Polizeidepartement EJPD, Umsetzung der Abzocker-Initiative: Verordnung tritt am 1. Januar 2014 in Kraft (Nov. 20, 2013), http://www.ejpd.admin.ch/content/ejpd/de/home/ dokumentation/ mi/2013/2013-11-20.html. Swiss voters did, however, reject proposed caps that would have limited executive pay to twelve times that of the lowest paid worker. Jack Ewing, *Swiss Voters Decisively Reject a Measure to Put Limits on Executive Pay*, N.Y. TIMES, Nov. 24, 2013, *available at* http://www.nytimes.com/2013/11/25/business/swiss-reject-measure-to-curb-executive-pay.html?_r=0.

5. We are more precise about these issues than some other recent empirical studies. *See, e.g.*, Riccardo Correa & Ugur Lel, *Say on Pay Laws, Executive Compensation, Pay Slice, and Firm Value Around the World* (Working Paper 2013), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2243921 (incorrectly claiming that Switzerland had adopted Say on Pay legislation as of June 2013); Kevin J. Murphy, *Executive Compensation: Where We Are, and How We Got There*, *in* 2

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What is the justification for adopting these rules? The answer to this question turns in large part on the prevailing share ownership structure of corporations in the country in question. For countries where most corporations have dispersed ownership structures, like the U.S., the U.K. and Australia, proponents have claimed that these votes will allow shareholders to monitor management and thereby reduce the agency costs of the separation of ownership and control in public companies.[6] Advocates argued that institutional investors, assisted by third-party voting advisors, would overcome collective action problems, inform themselves about corporate performance and intelligently evaluate the executive pay packages being proposed by corporate boards. Boards would, in turn, respond by better engaging with their investors and providing them with more information, tie executive pay more closely to performance and show greater restraint in the compensation awards.[7] Opponents of Say on Pay denied that any of these possible benefits would result and instead claimed that the entire effort was misplaced.[8]

In concentrated ownership countries,[9] such as the Netherlands, Germany, Sweden, and Belgium, the story is more nuanced. The existence of controlling shareholders at most companies in these countries means that there already is close monitoring of executive pay levels by a motivated owner.[10] Thus, at first blush, there seems to be little reason for these countries to have adopted Say on Pay voting requirements. However, on closer examination, we find several other reasons for these changes, including: increased ownership dispersion at larger public companies creating a need for a new monitor of executive pay; strong support of such legislation by foreign institutional investors whose ownership interests in EU-based firms has increased dramatically in recent years; social

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HANDBOOK OF THE ECONOMICS OF FINANCE 211, 211 (George Constantinides, Milton Harris & Rene Stulz eds., 2012) (incorrectly stating that France has enacted a binding Say on Pay vote).

6. Randall S. Thomas, Alan R. Palmiter & James F. Cotter, *Dodd-Frank's Say on Pay: Will It Lead to a Greater Role for Shareholders in Corporate Governance?*, 97 CORNELL L. REV. 1213, 1232 (2012)

7. *Id.* at 1231–33.

8. Stephen M. Bainbridge, *Is 'Say on Pay' Justified?*, 32 REG. 42 (2009).

9. By concentrated ownership countries, we mean jurisdictions in which most public firms have controlling shareholders or control groups. Randall S. Thomas, *Explaining the International CEO Pay Gap: Board Capture or Market Driven?*, 57 VAND. L. REV. 1171, 1196 (2004) ("In most foreign countries, stock ownership is much more concentrated than in the United States, and many firms are controlled by majority shareholders."). For a more complete discussion in the context of Europe, see THE CONTROL OF CORPORATE EUROPE (Fabrizio Barca & Marco Becht eds., 2001).

10. Lucian A. Bebchuk, Jesse Fried & David Walker, *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751, 839–40 (2002); Thomas, *supra* note 9, at 1196 (arguing that international pay gap rests on market driven factors).

pressures against rising levels of income inequality; political responses by left-leaning parties to these social pressures by the introduction of Say on Pay legislation; and the presence of important state-owned enterprises in some of these countries that give politicians an important role in setting executive pay.

The effects of Say on Pay votes are harder to summarize because they vary across nations. However, several general statements can be made. First, when Say on Pay votes are held, shareholders vote to approve the pay levels, pay composition, and pay policies, at almost all companies by very wide margins. Second, third-party voting advisors, such as Institutional Shareholder Services ("ISS"), pay a crucial role in informing institutional investors about executive compensation practices and packages. These advisors' recommendations for, or against, a company's pay plan may also carry significant weight with their institutional clients, and can dramatically impact the outcome of a vote. Third, Say on Pay's strongest effect has been felt at companies that exhibit poor performance with relatively high levels of pay.[11] Fourth, when companies receive low levels of shareholder support in a vote, directors frequently contact their investors to better explain their policies, thereby giving shareholders greater input into pay issues. Fifth, Say on Pay votes appear to have had little long-term impact on executive pay levels, while research on their impact on shareholder value tends to show a small positive impact, although some studies find no, or negative, effects.

Overall, we conclude that Say on Pay is here to stay. In fact, if the recent experience of the Swiss popular referendum in favor of a binding vote on executive compensation is any gauge, then it seems likely to appear in more countries over time. Thus, in the final Part of this Article, we look at the future of Say on Pay. We hypothesize that if boards continue to increase pay levels over time, then countries with advisory votes will move to make them binding votes. This already has been the case in the U.K. and Australia. Moreover, some legislatures will feel it necessary to impose hard-law regulations on compensation practices, either directly on pay levels and composition as the EU already did and is further threatening to do for banks,[12] or indirectly as the Australians have

11. Correa & Lel, *supra* note 5, at 14.

12. *See* Council Directive 2013/36, of the European Parliament and of the Council of 26 June 2013 on Access to the Activity of Credit Institutions and the Prudential Supervision of Credit Institutions and Investment Firms, Amending Directive 2002/87/EC and Repealing Council Directives 2006/48/EC and 2006/49/EC, art. 92–94, 2013 O.J. (L 176) 338, 386–89 (EU).

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done by attaching severe consequences to boards' failure to respond to repeated high levels of shareholder dissent in Say on Pay votes.[13]

This Article proceeds as follows. In Part I, we provide an overview of the current state of Say on Pay in the U.S., U.K., Australia, Belgium, France, Germany, Sweden and the Netherlands. Part II distills the experiences of these nations to develop a set of explanatory factors for why Say on Pay legislation has been adopted, or seems likely to be adopted, in these countries. The final Part of this Article contains our predictions about the future of Say on Pay in these and other countries.

I. DESCRIPTION OF THE SAY ON PAY REGIMES: LEGAL RULES AND VOTING OUTCOMES

While Say on Pay has been the topic of several empirical studies at both the national and international level, many of these papers do not clearly define Say on Pay. This is important because different kinds of shareholder votes coexist and it is a serious mistake to treat them all as equivalent.[14] In our study, we define Say on Pay as: (1) a recurring, mandatory,[15] (2) binding or advisory shareholders' vote, (3) provided by law,[16] that (4) directly or indirectly through the approval of the remuneration system, remuneration report or remuneration policy, (5) governs the individual or collective global remuneration package of the executives or managing directors of the corporation.[17] As we will see, not all countries that permit shareholder votes on executive remuneration issues provide those investors with a Say on Pay vote.

We begin with a detailed discussion of the Say on Pay regimes adopted, or proposed, in eight of the most important industrialized countries in the world: the U.S., the U.K., Australia, Belgium, France, Germany, Sweden and the Netherlands. While there has been some

13. See *infra* Part I.C for further discussion of the Australian rules on Say on Pay.

14. One recent study correctly identified eleven European countries with some kind of Say on Pay regulations. *See* Roberto Barontini, Stefano Bozzi, Guido Ferrarini & Maria-Cristina Ungureanu, *Directors' Remuneration Before and After the Crisis: Measuring the Impact of Reforms in Europe*, *in* BOARDS AND SHAREHOLDERS IN EUROPEAN LISTED COMPANIES 251, tbl.1 (2013). However, Correa and Lel included only six of these countries in their empirical analysis of Say on Pay. Correa & Lel, *supra* note 5, at tbl.1.

15. Our definition excludes legal provisions that give companies the option of providing shareholders a vote on the remuneration of directors (as is the case in Germany).

16. This means that we exclude a shareholder vote that might be undertaken as the result of a Comply or Explain corporate governance code (even if mandatory), which is not law (as is the case in France).

17. Under our definition, shareholder approval of only a part of the executive's remuneration package, like the granting of stock options, is not a Say on Pay vote.

research conducted in the first three countries mentioned, almost nothing has been written about the experiences of the Continental European countries.[18] As a result, much of the statistical evidence that we report on these five countries is derived from data that we have hand collected and put into tables.

A. Say on Pay in the U.S.

1. Development

Say on Pay in the U.S. grew out of precatory shareholder-sponsored Rule 14a-8[19] proposals submitted to public companies for inclusion on their proxy statements.[20] Beginning in the 2006 proxy season, the American Federation of State, County, and Municipal Employees (AFSCME) started submitting these proposals, which recommended that the corporate boards at the targeted companies give shareholders a nonbinding vote on the companies' pay for their top executives.[21]

These early Say on Pay shareholder proposals were uniformly opposed by management but received significant shareholder support.[22] Management argued that the board of directors, not shareholders, was responsible for setting executive compensation. In their eyes, shareholder input would only impede the board's ability to act effectively. Initially, boards ignored Say on Pay proposals—even those supported by a majority of shareholders.[23]

In 2008, in response to public concerns about the financial crisis, Congress put Say on Pay on its legislative agenda. The Emergency Economic Stabilization Act of 2008 (EESA) required Troubled Asset Relief Program (TARP) fund recipients to provide their shareholders with

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18. A notable exception is the comparative work in Barontini et al., *supra* note 14 (providing both empirical data on the development of executive pay in large European companies and the general state of the art on Say on Pay rules in European countries).

19. 17 C.F.R. § 240.14a-8.

20. Thomas et al., *supra* note 6, at 1218.

21. Charles Nathan, *"Say on Pay" Shareholder Advisory Votes on Executive Compensation: The New Frontier of Corporate Governance Activism*, LATHAM & WATKINS M&A COMMENT. (Nov. 2007), http://www.lw.com/upload/pubContent/_pdf/pub2039_1.pdf. *See also* Sandeep Gopalan, *Say on Pay and the SEC Disclosure Rules: Expressive Law and CEO Compensation*, 35 PEPP. L. REV. 207, 220–21 (2008).

22. Thomas et al., *supra* note 6, at 1219–20.

23. Marcel Kahan & Edward Rock, *Embattled CEOs*, 88 TEX. L. REV. 987, 1012 (2010).

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an advisory vote on the pay for the company's executives.[24] In 2009, the financial stimulus plan continued the Say on Pay requirement for financial firms with outstanding TARP debts.[25]

To implement this new legislation in 2009, the SEC required an advisory shareholder vote on executive pay packages of TARP recipients.[26] During the 2010 proxy season, about 280 financial firms held Say on Pay votes.[27] The EESA mandate increased the number of firms subject to advisory Say on Pay votes beyond those shareholders identified as having "bad" compensation.[28]

The 2010 proxy season saw shareholders at TARP-funded firms vote in support of management-sponsored Say on Pay proposals with an average support level of 88.7%.[29] This high level of shareholder support for executive pay policies is interesting since in 2010 most of the Say on Pay votes were held at financial firms that had fared poorly during the financial crisis.

2. Dodd–Frank Requirements

Advisory Say on Pay for top executives' compensation was made universal for public companies by section 951 of the Dodd-Frank Act.[30] Under section 951, the SEC provided detailed requirements that identify both the form of the Say on Pay proposal and the executive officers whose compensation is subject to a shareholder vote.[31] Say on Pay votes are now

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24. The Troubled Asset Relief Program, established by the Emergency Economic Stabilization Act of 2008 (EESA), required that companies with outstanding funds provide an advisory vote to their shareholders. *See* EESA, Pub.L. 110-343, § 111(a), (codified at 12 U.S.C. § 5221(e) (2008)).

25. The American Recovery and Reinvestment Act of 2009, while amending some aspects of EESA, left intact the "say on pay" requirements. Pub. L. No. 111-5, 123 Stat. 517 (2009). Thus, financial companies with outstanding TARP funds are required to submit executive pay to a shareholder vote under both TARP and Dodd–Frank. The SEC has made clear that only one vote, however, is necessary to satisfy both statutory requirements. *See* SEC Final Rule, 17 C.F.R. §§ 229, 240, 249 (2011), *available at* http://www.sec.gov/rules/final/2011/33-9178.pdf (vote under EESA is "effectively" the same as required by Dodd–Frank). Given that TARP recipients are required to conduct a "say on pay" vote annually, the SEC has exempted them from a vote on the frequency of "say on pay." *See id.* at 57–58.

26. *See* Shareholder Approval of Executive Compensation of TARP Recipients, 17 C.F.R. § 240 (2010) (adopting Rule 14a-20 to require TARP recipients to provide a separate non-binding shareholder vote to approve compensation of executives whenever shareholders vote at an annual meeting involving election of directors).

27. Thomas et al., *supra* note 6, at 1223.

28. *Id.* at 1224.

29. *Id.* at tbl.2.

30. Dodd–Frank Act, Pub. L. No. 111-203, 124 Stat. 1899 (2010).

31. Thomas et al., *supra* note 6, at 1225.

required at shareholder meetings held after January 21, 2011 at public companies with a $75 million public equity float or more.[32]

Only the pay packages of a company's executive officers named in the company's proxy compensation table are subjected to the vote.[33] The vote is up or down as to the overall compensation package as described in the Compensation Discussion and Analysis (CD&A) section of the proxy statement,[34] and does not allow shareholders to directly voice an opinion on specific elements of executive compensation (such as bonuses, stock options, retirement pay, performance incentives).[35]

3. Impact of Say on Pay

In the 2011 proxy season, shareholders voted on these management proposals at about 2200 US public companies.[36] The results showed several clear trends. First, shareholders strongly supported existing pay practices at most firms with Say on Pay votes garnering on average 91.2% support. Second, management proposals were voted down only 1.6% of the time,[37] and when that happened it was often based on by pay-for-performance concerns. Third, shareholder votes were highly correlated to company share returns and CEO pay, with low returns and high CEO pay resulting in lower Say on Pay support. Fourth, negative Say on Pay recommendations by third-party voting advisors prompted many

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32. SEC Final Rule, 17 C.F.R. § 240.14a-21(b) (2011), *available at* http://www.sec.gov/rules/final/2011/33-9178.pdf. Smaller reporting companies become subject to the Say on Pay voting requirement for annual meetings after January 21, 2013. *Id.*

33. *See id.* § 240.14a-21(a) ("say on pay" vote required at annual shareholder meetings at which directors are elected for named executives whose compensation is disclosed pursuant to Item 402 of Regulation S-K). The compensation of directors is not subject to a mandatory "say on pay" vote. *See id.*

34. The SEC rule does not require that the management-submitted "say on pay" proposal be phrased in a particular way, though it must indicate that the proposal seeks a shareholder vote "to approve the compensation of executives as disclosed pursuant to Item 402 of Regulation S-K." *Id.* at 19 (quotations and alterations omitted). A suggested proposal calls on shareholders to approve "compensation paid . . . as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis, compensation tables and narrative discussion." *Id.* at 19 n.68. A vote to approve only compensation policies and procedures would not pass muster. *Id.* at 19–20.

35. *See id.* § 240.14a-21(a). In addition, the SEC added a comment to Rule 14a-8 that companies will be allowed to exclude shareholder-submitted proposals under the rule if the shareholder proposes a "say on pay" vote with "substantially the same scope the say-on-pay vote required by Rule 14a-21(a) . . . ." Thomas et al., *supra* note 6, at 44–45.

36. INST'L S'HOLDER SERVS., PRELIMINARY 2011 U.S. POSTSEASON REPORT 2. (updated Aug. 8, 2011). Equilar, a leading provider of data on executive pay, counted 2252 from the Russell 3000 as of June 30, 2011. EQUILAR, AN ANALYSIS OF VOTING RESULTS AND PERFORMANCE AT RUSSELL 3000 COMPANIES 5 (July 2011), http://www.equilar.com/knowledge-network/research-articles/2011/pdf/Equilar-Voting-Analytics-July2011.pdf.

37. Thomas et al., *supra* note 6, at 1248.

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companies to modify their disclosure filings or to change their pay practices (sometimes retroactively) to win support.[38]

An important question is what effect Say on Pay voting has had on shareholder value. Several studies attempt to measure this effect. Cunat, Gine and Guadalupe study Rule 14a-8 advisory shareholder proposals from 2006 to 2010 that request that companies permit their shareholders to vote on executive compensation at the firm.[39] They examine the immediate effect on firm stock market returns as well as longer-term effects on CEO compensation, accounting performance, productivity and firm policies. They find that on the day of the shareholder vote, if Say on Pay proposals receive more than 50% shareholder approval, the company experiences an abnormal return of 2.4% relative to one whose vote fails.[40] This study reports that where voting crosses the 50% threshold, there is a 50% higher likelihood of being implemented by the firm in question.[41] Further, firms implementing Say on Pay "have higher growth in earnings per share, return on assets, return on equity and Tobin's Q one year after the vote."[42] However, they find only small effects on executive compensation with a 4% reduction in salary increases.[43] They suggest that Say on Pay "serves to monitor and incentivize CEOs to deliver better firm performance by providing a clear mechanism for shareholders to voice their opinions, as confirmed by major improvements in shareholder value and firm performance among the firms in our sample."[44]

Other empirical research looking at the effect of Say on Pay on firm value uses event studies. One set of studies examines stock market reactions around regulatory events related to enactment of Say on Pay requirements. Ferri and Maber find small, positive price reactions to Say on Pay regulation in the U.K., particularly in firms with excess pay and controversial compensation practices.[45] There are similar findings as to the Congressional adoption of the U.S. Say on Pay legislation, although there

38. *Id.* at 1256–59.

39. Vincente Cunat, Mireia Gine & Maria Guadalupe, *Say Pays! Shareholder Voice and Firm Performance* (European Corporate Governance Institute (ECGI) Fin. Working Paper No. 373), *available at* http://ssrn.com/abstract=2240410.

40. *Id.* at 4.

41. *Id*.

42. *Id.* at 5.

43. *Id*.

44. *Id.* at 5–6. By comparison, Cai and Walkling find no stock price reaction to Rule 14a-8 proposals around the proxy filing dates and annual meeting dates. Jie Cai & Ralph A. Walkling, *Shareholders' Say on Pay: Does It Create Value?*, 46 J. FIN. & QUANTITATIVE ANALYSIS 299, 329–30 (2011).

45. Ferri & Maber, *supra* note 3, at 559.

is not unanimity on this point.[46] A second set of event studies examines the effect of Say on Pay induced compensation changes on stock prices finding either no stock price reaction[47] or small negative effects.[48]

Another recent study by Iliev and Vitanova examines the announcement of the SEC rules that gave smaller firms an additional two years before being subjected to the new requirement imposed on larger public companies.[49] They find that the announcement of this rule led to a positive 1.5% three day return for firms that were required to hold a Say on Pay vote versus those that were not.[50]

In the eyes of its supporters, Dodd–Frank's mandated shareholder votes have also focused management on shareholders' concerns, increased shareholder participation in corporate governance, and opened lines of communication between management and shareholders (and proxy advisory firms) regarding executive compensation.[51] Management at many companies made changes to the substance and disclosure of their pay programs in an attempt to more clearly align pay to performance.[52] Furthermore, many companies revised the content of the CD&A filed with the annual meeting proxy materials. At many companies whose pay programs received negative Say on Pay recommendations by proxy advisory firms, directors connected with shareholders following an "against" recommendation.[53] Changes in corporate governance behavior—

46. *See* Cai & Walkling, *supra* note 44, at 312–13 (finding positive and statistically significant stock price increase in firm values at companies with high abnormal CEO compensation, or low pay-for-performance sensitivity, within the three days surrounding the House of Representatives' passage of Say on Pay legislation); *but see* David F. Larcker, Gaizka Ormazabal & Daniel J. Taylor, *The Market Reaction To Corporate Governance Regulation*, 101 J. FIN. ECON. 431, 432 (2011) (Say on Pay legislation has an insignificant market reaction).

47. Yonca Ertimur, Fabrizio Ferri & David Oesch, *Shareholder Votes and Proxy Advisors: Evidence from Say on Pay*, 51 J. ACCT. RES. 951, 955 (2013) (no stock price reaction around compensation changes made after the vote explicitly in response to Say on Pay votes).

48. David F. Larcker, Allen McCall & Gaizka Ormazabal, *The Economic Consequences of Pay Advisor Say-on-Pay Voting Policies* 6 (Rock Ctr. for Corporate Governance at Stanford Univ. Working Paper No. 119; Stanford Univ. Graduate Sch. of Bus. Research Paper No. 14-27 (2105R), 2013), *available at* http://ssrn.com/abstract=2101453 (compensation changes made before the vote associated with a negative abnormal return of -0.44%); *see also* Christopher Armstrong, Ian D. Gow & David F. Larcker, *The Efficacy of Shareholder Voting: Evidence from Equity Compensation Plans*, 51 J. ACCT. RES. 909 (2013) (arguing that shareholder votes have little effect on firms' incentive-compensation policies).

49. Peter Iliev & Svetla Vitanova, *The Effect of the Say-on-Pay Vote in the U.S.* 3 (Pa. State Univ. Working Paper, 2013), *available at* http://ssrn.com/abstract=2235064.

50. *Id.*

51. Luis A. Aguilar, Comm'r, U.S. Sec. & Exch. Comm'n, Speech to Social Investment Forum (June 10, 2011).

52. *Id.*

53. *Id.*

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such as more complete disclosure of pay-for-performance policies and the reversal of specific, controversial pay practices—inaugurated by Say on Pay in 2011 continued apace in 2012 and 2013.

B. U.K. Say on Pay

1. Early Legislation

Decades of perceived excess executive remuneration and "rewards for failure" led to the evolution of Say on Pay legislation in the U.K.[54] Effective August 1, 2002, the U.K. became the first country to adopt mandatory nonbinding shareholder votes on director compensation (Say on Pay), through the Directors' Remuneration Report (DRR) Regulations.[55] In 2003, the first year of mandatory advisory votes in the U.K., shareholders at GlaxoSmithKline became the first to vote down their company's compensation report, by the slim margin of 50.72%.[56] Specifically, shareholders objected to an estimated $35 million golden parachute for the Philadelphia-based CEO.[57] Hailing it as a "landmark in corporate governance," "[s]ome British activists think it may mark the moment when British capitalism decided to stop converging with its American counterpart."[58]

However, in the overwhelming number of cases, shareholders vote in favor of management-presented compensation reports. One study suggests less than 10% of shareholders abstain from, or vote against, compensation reports.[59] In fact, between 2003 and 2009, only nine companies had their Say on Pay proposal defeated, and all but the Royal Bank of Scotland and GlaxoSmithKline were relatively small firms.[60] Furthermore, between

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54. Ferri & Maber, *supra* note 3, at 1.

55. Walid M. Alissa, *Boards' Response to Shareholders' Dissatisfaction: The Case of Shareholders' Say on Pay in the UK* 7 (Pennsylvania State University Working Paper May 2009), *available at* http://papers.ssrn.com/ sol3/papers.cfm?abstract_id=1412880; STEPHEN DEANE, WHAT INTERNATIONAL MARKETS SAY ON PAY: AN INVESTOR PERSPECTIVE 7 (2005); Ferri & Maber, *supra* note 3, at 1. The regulations become an amendment to the U.K. Companies Act. Jeffrey N. Gordon, *"Say on Pay": Cautionary Notes on the UK Experience and the Case for Shareholder Opt-in*, 46 HARV. J. ON LEGIS. 323, 342 (2009); Cheffins & Thomas, *supra* note 3, at 301.

56. DEANE, *supra* note 55, at 5.

57. Gordon, *supra* note 55, at 342.

58. DEANE, *supra* note 55, at 5.

59. *See* Martin J. Conyon & Graham V. Sadler, *Shareholder Voting and Directors' Remuneration Report Legislation: Say on Pay in the UK* 5 (Cornell Univ. Sch. of Indus. & Labor Relations, Compensation Res. Initiative Paper No. 2009-004, 2009), *available at* http://digital commons.ilr.cornell.edu/cri/2.

60. Jeremy Ryan Delman, Note, *Survey: Structuring Say-on-Pay: A Comparative Look at Global Variations in Shareholder Voting on Executive Compensation*, 2010 COLUM. BUS. L. REV. 583, 610.

2002 and 2007, only sixty-four out of 596 reporting companies received dissent of more than 20%.[61]

2. The Effects of Nonbinding Say on Pay in the U.K.

Since its enactment in 2002, the Directors' Remuneration Report (DRR) regulations have been the subject of much academic scholarship.[62] Generally, empirical studies suggest that no change in the executive pay growth rate occurred after the adoption of the U.K. regulations.[63] However, the "Say on Pay" regulation may have a "moderating effect on the level of CEO compensation *conditional upon poor performance*."[64] Shareholders dissent more where CEO compensation is above the "average excess compensation"[65] and where pay is not closely tethered to performance.[66] Studies suggest, however, that a board's responsiveness to such shareholder dissent is mixed.[67]

Empirical results further show that Say on Pay regulation "was accompanied by positive stock price reactions at firms with controversial pay practices and, more specifically, practices that weaken penalties for poor performance, consistent with investors perceiving say on pay as a value-creating governance mechanism."[68] This suggests shareholders view the new regulation as a "value enhancing monitoring mechanism."[69]

Even with most reports receiving over a 90% shareholder approval rate, compensation reports attract the single highest dissention rate among shareholders when contrasted with shareholder voting patterns on any

61. *Id.*

62. *E.g.*, Alissa, *supra* note 55; Mary Ellen Carter & Valentina Zamora, *Shareholder Remuneration Votes and CEO Compensation Design* (AAA 2008 MAS Meeting Paper, 2007), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1004061; Conyon & Sadler, *supra* note 59; Ferri & Maber, *supra* note 3; Kym Sheehan, *Say on Pay and the Outrage Constraint* (The Executive Remuneration Reporter Working Paper, 2010), *available at* http://ssrn.com/abstract=1679622 (updating 2007 study).

63. Ferri & Maber, *supra* note 3, at 554; *see also* DEANE, *supra* note 55, at 9 ("Despite these pay-for-performance successes, observers in . . . the U.K. . . . note that executive pay levels are still ratcheting upward.").

64. Ferri & Maber, *supra* note 3, at 555.

65. *See* Alissa, *supra* note 55, at 23 (indicating firms reduce compensation more often when such firms are the average excess compensation).

66. Carter & Zamora, *supra* note 62, at 24.

67. *See* Alissa, *supra* note 55, at 35 (arguing boards are more responsive at levels of above average excess compensation); Carter & Zamora, *supra* note 62, at 23 (acknowledging lag in responsiveness). *But see* Conyon & Sadler, *supra* note 62, at 29 ("There is little evidence that shareholder say on pay has consequences for subsequent CEO compensation practices.").

68. Ferri & Maber, *supra* note 3, at 534–35.

69. *Id.* at 559.

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other similar proposals.[70] Significantly, votes against DRR exceed those shareholder votes against the reelection of directors of firms.[71]

Studies do seem to suggest that, at the margin, shareholders use their votes on DRR to convey their dissatisfaction with excessive pay practices.[72] One paper by Alissa suggests that shareholders are in dissention when pay and performance are "mismatched."[73] Moreover, the paper recognizes a statistically significant correlation in excess compensation and dissenting shareholder votes.[74] Similarly, the Carter and Zamora study indicates shareholder disapproval is highest when CEO salary is higher, there is weaker pay-for-performance sensitivity in bonus pay, and there is greater potential dilution from stock-based compensation, particularly in stock option pay.[75] Sheehan similarly concludes her U.K. study by noting that "institutional investors use the *threat* of a negative vote to enforce compliance."[76]

Evidence regarding boards' responsiveness to shareholders' nonbinding votes is mixed. Ferri and Maber found that firms did respond to high shareholder dissention by "removing controversial provisions criticized as rewards for failure, such as long notice periods and retesting provisions for option grants."[77] Furthermore, their study found a "significant increase in the sensitivity of CEO pay to poor performance," especially where firms experienced high shareholder dissention at a first

70. Conyon & Sadler, *supra* note 62, at 21–22. The study contrasted DRR dissention with negative shareholder votes on ten other resolutions regarding: director elections, major acquisitions or disposals, appointing or approving auditors' remuneration, equity decisions, the company generally (e.g., name change, wind up, delisting, or donation authorization), dividend distribution, articles of association amendments, more specific remuneration issues, contingent votes, and accepting other reports or accounts. *Id.* at 16.

71. *Id.* at 22. For example, amidst the 2003 GlaxoSmithKline shareholder voting drama regarding the pay of CEO Dr. Grenier, shareholder dissent for the first time exceeded 50 percent as to a DRR resolution, but the re-election of the CEO attracted 75 percent shareholder support. *Id.* at 20–21. Illustrating "shareholders are prepared to signal dissatisfaction by voting against pay, but not to the degree of removing directors." *Id.* at 21.

72. *See* Sheehan, *supra* note 62, at 29 (offering evidence that shareholders are more likely to vote against DRR resolutions than board election as evidence that "DRR is a way to signal shareholder dissatisfaction to the firm about pay"); Alissa, *supra* note 55, at 23 (offering her study as evidence that shareholders disapprove mismatches between pay and performance such that "[t]he higher the mismatch, the greater the dissatisfaction expressed by shareholders").

73. Alissa, *supra* note 55, at 23.

74. *Id.* at 16, 23–24 (expressly ruling out the possibility shareholders vote based on pure "level of compensation" such that "higher overall levels of total compensation would result in greater shareholders dissatisfaction").

75. Carter & Zamora, *supra* note 62, at 19–24.

76. Sheehan, *supra* note 62, at 18–19.

77. Ferri & Maber, *supra* note 3, at 559. The authors do note that their evidence is the result of a study done only from changes in disclosed provisions of compensation contracts and therefore may not capture the "full effect of say on pay compensation practices." *Id.* at 547.

vote and at firms with excess CEO pay before the Say on Pay regulation.[78] Consistent with the other relevant studies, however, Ferri & Maber confirm that after controlling for performance, there is no change in the growth rate of CEO pay.[79]

Providing a somewhat more tempered result, Carter and Zamora indicate, "when given the contractual opportunity . . . boards do respond with lower [compensation] increases than other firms."[80] Their paper claims that when executives respond they "curb[] salary increases and dilution from stock option grants" thereby improving CEO bonus PPS links.[81]

While Alissa finds "no evidence for the hypothesis that the board responds to shareholders' dissatisfaction by changing excess compensation," his results do indicate that where CEO excess pay is above the mean, boards respond by reducing excess compensation.[82] Alternatively, the second prong of Alissa's study suggests that boards similarly respond to shareholder pressure and dissatisfaction by "forcing" the CEO out of office.[83] Therefore, this bifurcated test leads Alissa to conclude that boards are responsive to shareholders' votes.[84]

Conversely, the Conyon study shows "little evidence of a relation between CEO pay and shareholder dissent on the directors' remuneration report."[85] Furthermore, the study states no evidence exists that CEO pay is negatively correlated with previous shareholder voting dissent in firm's greater "excess pay."[86] However, Ferri and Maber offer an interesting insight (predicted by many) to rebut this negative view of a board's responsiveness, suggesting that "many firms removed this provision *ahead* of the vote, presumably in an attempt to avoid voting dissent and consistent with institutional investors' preference for 'bargaining in the shadow.'"[87]

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78. *Id.*
79. *Id.* at 554.
80. Carter & Zamora, *supra* note 62, at 23.
81. *Id.* at 24.
82. Alissa, *supra* note 55, at 26–27.
83. *Id.* at 27–29 (defining "forcing out of office" and providing results).
84. *Id.* at 35.
85. Conyon & Sadler, *supra* note 62, at 25.
86. *Id.*
87. Ferri & Maber, *supra* note 3, at 546.

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3. New Legislation Implementing Binding Say on Pay

In June 2012, the U.K.'s Department for Business Innovation & Skills released a consultation proposing compensation reporting regulations and implementation of binding Say on Pay in the U.K. for companies with shares on the Financial Services Authority's Official List[88] as well as all U.K. companies listed on the NYSE, the NASDAQ, or with shares listed in another EEA state, beginning in October 2013.[89] Under its auspices, U.K. companies will now be required to put to an annual binding shareholder vote its "director remuneration policy, including its approach to termination payments."[90] If a company fails a binding vote on compensation, "it must continue using the last policy approved by shareholders until a revised policy is approved."[91] The new proposal's expanded disclosure requirements require companies to set out their exit payment approach in the compensation policy report, subject to the binding shareholder vote.[92] This proposal[93] was recently enacted into law.[94]

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88. Danielle Harris, *UK Reform on Director Pay*, GOVERNANCE, Sept. 2012, at 8 (noting that it is irrelevant if the shares have a premium or standard listing).

89. *Id.*; DEP'T FOR BUSINESS INNOVATION & SKILLS, DIRECTORS' PAY: CONSULTATION ON REVISED REMUNERATION REPORTING REGULATIONS 15 (June 2012).

90. *Binding Shareholder Say-on-Pay Vote on Route to Reality in the UK: US Companies Take Note*, CLEARY GOTTLIEB 4 (July 9, 2012), http://www.cgsh.com/files/News/3b4b3be5-0f26-49ce-9c95-0bfd5207e8df/Presentation/NewsAttachment/2339ed13-5b2d-4e59-9830-0ce4ed80a645/CGSH%20Alert%20-%20Gov%20UK%20Binding%20Say%20on%20Pay.pdf.

91. *Id.* at 6.

92. Marisa Anne Pagnattaro & Stephanie Green, *"Say on Pay": The Movement to Reform Executive Compensation in the United States and European Union*, 31 NW. J. INT'L L. & BUS. 593 (2011).

93. Draft Statutory Instrument: the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013, Mar. 13, 2013, *available at* https://www.gov.uk/government/publications/draft-statutory-instrument-on-directors-remuneration-the-large-and-medium-sized-companies-and-groups-accounts-and-reports-amendment-regulations-2013 (last visited June 15, 2013).

94. Enterprise and Regulatory Reform Act, 2013, c. 24, (Eng.) *available at* http://www.legislation.gov.uk/ukpga/2013/24/enacted; Enterprise and Regulatory Reform Act, 2013, c. 24, § 79 (Eng.) *available at* http://www.legislation.gov.uk/ukpga/2013/24/part/6/crossheading/payments-to-directors-of-quoted-companies/enacted (displaying the remuneration portion of the Act).

C. Say on Pay in Australia

1. Overview

Executive pay in Australia grew greatly between 1993 and 2008, showing the largest growth between the mid-90s and 2000.[95] This growth in executive compensation is largely attributable to increases in incentive pay.[96] However, even as Australian pay rates increased significantly, absolute CEO pay level remained well below Australia's peers the U.S. and the U.K., aligning Australia with many smaller European countries.[97]

In response to shareholders' and other market participants' "general unease" about executive pay, the Australian government inserted section 250R (2) into the Corporations Act of 2001 (Cth).[98] This section required a nonbinding shareholder vote on all listed companies' remuneration reports, at the annual general meeting (AGM).[99]

Professor Sheehan studied the Australian experience during 2005 to 2008 using voting data from 109 companies listed on the S&P/ASX 200.[100] She concluded that the data showed a progressively higher rate of shareholder dissention over the years studied. This is consistent with data in the 2009 Productivity Commission Report, which claims that the global financial crisis was a leading cause of high negative votes at companies.[101]

After the financial crisis, Australia's Productivity Commission reviewed the history and regulatory framework of Australia's executive remuneration regulations, and made several important recommendations.[102] On June 20, 2011, the Australian Senate passed the Corporations Amendment (Improving Accountability on Director and

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95. PRODUCTIVITY COMM'N, EXECUTIVE REMUNERATION IN AUSTRALIA xv–xvi, xvi fig.1 (2009) (showing likelihood executive compensation at Australia's largest public companies grew by as much as 300%).

96. *Id.* at xvii (noting the "long-term" incentives tripled between 2004 and 2007).

97. *Id.* at xix–xx.

98. Larelle Chapple & Blake Christensen, *The Non-Binding Vote on Executive Pay: A Review of the CLERP 9 Reform*, 18 AUSTL. J. CORP. L. 263, 263 (2005).

99. *Id.* (section 250R(3) speaks to the "nonbinding" nature of the vote).

100. Kym Sheehan, *Say on Pay and the Outrage Constraint*, EXECUTIVE REMUNERATION REP. (Sept. 20, 2010) [hereinafter Sheehan, *Say on Pay*], *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1679622; Kym Sheehan, *Is the Outrage Constraint an Effective Constraint on Executive Remuneration? Evidence from the UK and Preliminary Results from Australia*, EXECUTIVE REMUNERATION REP. (Mar. 18, 2010) [hereinafter Sheehan, *Outrage Constraint*], *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_ id=974965.

101. PRODUCTIVITY COMM'N, *supra* note 95, at 282–86.

102. *Id.* at xxxiv (providing a table summarizing recommendations and with the targeted benefits of each).

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Executive Remuneration) Bill 2011,[103] which included substantial changes to prior Say on Pay provisions.

2. Say on Pay: The Two-Strike Rule

An explanatory memorandum, released by the Australian Parliament, weighed the positive and negatives of a nonbinding shareholder vote. The memorandum recognized that nonbinding shareholder votes might provide benefits, such as "increased dialogue between companies and shareholders on remuneration issues."[104] Furthermore, it openly acknowledged evidence that "some boards are responsive to the non-binding vote, and that the opportunity for shareholders to put forward their views is having a positive impact on remuneration policies."[105] Still, the Australian Parliament was uncomfortable with existing legislation that imposed no penalty on nonresponsive boards in the face of a negative nonbinding shareholder vote (except the "nuclear option" of director removal).[106]

Australia similarly recognized significant deficiencies in the alternative—binding shareholder votes. Specifically, the memo noted that binding shareholder votes had the potential to "absolve directors of their responsibility to shareholders" regarding executive compensation, thereby undermining the broad authority of the board to make decisions. It further noted concern that a binding shareholder vote would "affect the competitiveness of Australian companies and their ability to attract and retain top executives."[107] After weighing its options, Australia settled somewhere in between: while resisting moving to a mandatory binding shareholder vote, the new regulations purport to strengthen a mandatory non-binding vote with the "Two-Strike Rule."[108]

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103. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth) (Austl.), *available at* http://www.comlaw.gov.au/Details/C2011A00042. For a helpful summary of the legislation, see *New Director and Executive Remuneration Legislation Passed by Parliament*, ERNST & YOUNG 1 (June 2011), *available at* http://www.ey.com/Publication/vwLUAssets/New_director_and_executive_remuneration_legislation/$FILE/Corporations%20Amendment_Improveration%20Bill%202011%20-%20FINAL.pdf. The private opinions submitted to the Treasury may be found at the treasury's archived site, http://archive.treasury.gov.au/contentitem.asp?ContentID=1960 *archived at* http://perma.cc/RS9U-TUKG.

104. Explanatory Memorandum, Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Bill 2011 (Cth) 5 (Austl.) [hereinafter *Explanatory Memorandum*], *available at* http://archive.treasury.gov.au/documents/1925/PDF/Explanatory_Memorandum.pdf.

105. *Id.*

106. *Id.*

107. *Id.* at 6.

108. *Id*. The Productivity Commissions inquiry concluded practical difficulties and risks precluded adoption of binding shareholder votes on pay. *Id.* at 5. The commission identified the

The Two-Strike Rule provides shareholders of listed companies an opportunity to "spill the board" if the company remuneration report receives a negative reception at two consecutive AGMs.[109] The "first strike" occurs when a company receives a "no" vote of 25% or more of the shareholder votes cast on its remuneration report.[110] Following a first strike, the company's subsequent remuneration report must explain the board's response and proposed action or inaction.[111]

At the next AGM, upon receiving a second consecutive "no" vote of 25% or more of the shareholders' votes cast on the remuneration report (the "second strike"), the shareholders will be required to vote on a "spill resolution" at the same AGM.[112] This spill resolution will determine whether the company's directors will need to stand for re-election at a "spill meeting."[113] If the spill resolution receives 50% or more of the eligible shareholder votes cast, the separate spill meeting must be held within 90 days.[114] The second strike and the spill resolution were intentionally separated to ensure that shareholders are not *discouraged* from voting against the remuneration report for fear of director removal.[115]

To ensure the effectiveness of the spill resolution following the first strike, in a company's meeting papers for their next AGM, a company must provide notice of the potential for a spill resolution at that AGM, in case a second strike triggers such a resolution.[116] Furthermore, following a passage of the spill resolution, a company must still provide the minimum notice period required by both the Corporations Act and any self-imposed

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uncertainty and delay stemming from the inability of finalizing executive contracts and certain possible operational disruptions, as two such risks. *Id.*

109. Blake Dawson (Ashurst), *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011*, at 3 (2011), *available at* www.ashurst.com/doc.aspx?id_Content=6930, *archived at* http://perma.cc/A4LS-L.

110. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), para 300A(1)(g); *see also Explanatory Memorandum*, *supra* note 104, at 6; Ernst & Young, *supra* note 103, at 2.

111. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), para 300A(1)(g); *see also Explanatory Memorandum*, *supra* note 104, at 6; Ernst & Young, *supra* note 103, at 2.

112. *Explanatory Memorandum*, *supra* note 104, at 7.

113. Ernst & Young, *supra* note 103, at 2.

114. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), s 250V; *see also Explanatory Memorandum*, *supra* note 104, at 6; Ernst & Young, *supra* note 103, at 2.

115. *Explanatory Memorandum*, *supra* note 104, at 7.

116. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), ss 249L(2); *see also Explanatory Memorandum*, *supra* note 104, at 7 (to clarify, the AGM that requires notice of the spill resolution is the AGM following the first strike AGM, at which the second strike vote would occur).

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notice period set out in the company constitution to ensure shareholders' ability to nominate and endorse board candidates at the special re-election meeting (spill meeting).[117]

At the spill meeting, all of the directors, except the managing director,[118] serving "when the resolution to make the directors' report" was considered, must stand for re-election. Furthermore, such directors cease to hold office at that time unless they are re-appointed by the shareholders.[119] However, if a vacating director is re-appointed, their term continues as though it were uninterrupted.[120] Such surviving directors serve the duration of their appointment from the date that they were last appointed to the board.[121] Also, at the spill meeting shareholders will vote on resolutions to appoint persons to the vacated positions.[122]

Section 250X disallows a complete board spill, requiring that at least the managing director and the two people receiving the highest portion of the votes, though not necessarily a majority, remain.[123] If two or more individuals have the same percentage of votes, the remaining director(s) may choose which of the candidates is appointed as a director, but this appointment must be approved at the company's next AGM.[124]

If the spill meeting does not convene by the end of the ninety-day period, each director in office at the end of such period is strictly liable.[125] Section 249CA of the Corporation's Act empowers any director of a listed company to call a meeting of the company's members, thus ensuring every

117. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), s 250W; *Explanatory Memorandum*, *supra* note 104, at 6–7.

118. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), ss 250V(1); *see also Explanatory Memorandum*, *supra* note 104, at 7 (ASX listing rules permit managing directors to hold office indefinitely and without re-election).

119. Dawson, *supra* note 109, at 3. However, if the directors that are up for re-election do not remain in office until the spill meeting or the (potentially) ninety days preceding it, then the meeting need not be held. *Id.* This is true whether or not the vacating directors' positions have been filled. *Id.* at 8.

120. *Id.* at 3.

121. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), s 250Y. This provision prevents directors from receiving a "fresh start through re-election vote as providing directors a fresh start. Explanatory Memorandum, *supra* note 104, at 9.

122. Dawson, *supra* note 109, at 3.

123. *Id.* at 4.

124. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), s 250X; *see also Explanatory Memorandum*, *supra* note 104, at 8–9.

125. *Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), ss 250W(5); *see also* Dawson, *supra* note 109, at 4. A single exception applies for directors who are appointed after the last date on which notice may be given for the spill meeting under § 249HA. *See also Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011* (Cth), s 250W(8).

director has the practical ability to avoid the offense.[126] Section 250U has a resetting mechanism that only allows consideration of a spill resolution at every second AGM.[127] This rule applies to remuneration report votes held after July 1, 2011, allowing a spill resolution to be triggered only where both strikes occur after that date.[128]

3. Initial (Mixed) Reactions to the Two-Strike Rule

One year after the enactment of the Two-Strike Rule, 28 (approximately 9%) of ASX 200 companies,[129] and 106 ASX companies overall,[130] received a first strike making them susceptible to a dangerous strike two in the next proxy season.[131] These numbers generated a wide range of responses from commentators with investor groups "warmly welcom[ing]" the new bill, while the Australian Institute of Company Directors referred to it as a "'heavy-handed black letter law approach' that would produce unnecessary red tape."[132]

A recent survey of the Australian-based law firm Allens Linklaters's listed company clients shows 72% express disapproval of the Two-Strike Rule suggesting "significant (AGM) reform" is necessary, with a majority

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126. *Explanatory Memorandum*, *supra* note 104, at 8.

127. Dawson, *supra* note 109, at 4.

128. Ernst & Young, *supra* note 103, at 2 (a no vote after July 1, 2011 results in the *first* strike); *Explanatory Memorandum*, *supra* note 104, at 8.

129. Matt Orsagh, *"Say on Pay" in Australia: Two Strikes and You're Out*, CFA INSTITUTE (Sept. 26, 2012), http://blogs.cfainstitute.org/marketintegrity/2012/09/26/say-on-pay-in-australia-two-strikes-and-youre-out/, *archived at* http://perma.cc/RG2H-556N.

130. Greg Dooley of Computershare Investor Services reports, 106 ASX companies received a first strike on their 2011 remuneration report, 14 of which he reports were ASX200 with 4 in the ASX100. *See* Greg Dooley, *2011 AGM season—Providing Clues to What Lies Ahead*, KEEPING GOOD COMPANIES, Mar. 2012, at 86–87, *available at* http://www.computershare.com/au/Investor%20 Services/CSA_Mar2012_AGM_Season.pdf *archived at* http://perma.cc/6H3-DNBG.

131. Several different estimates are in other reports. MALLESONS STEPHEN JAQUES, DIRECTIONS 2012: CURRENT ISSUES AND CHALLENGES FACING AUSTRALIAN DIRECTORS AND BOARDS 14 (2011), *available at* http://www.mallesons.com/Documents/Directions_2012.pdf, *archived at* http://perma.cc/HY5C-8K5S (stating that *at least* 60 companies total received a first strike during the 2011 proxy season); HENRY DAVIS YORK, TWO STRIKES RULE ENTERS ITS SECOND AGM SEASON 1 (Aug. 2012), *available at* http://www.hdy.com.au/Media/docs/HDY_Insight_Corporate%20Advisory_Aug%2012-bf5a0c01-fca6-485b-9e79-62f254bcdeb0-0.pdf, *archived at* http://perma.cc/U4V5-TVD7 (reporting over 100 listed companies received their first strike during the 2011 proxy season by attracting over 25% negative votes against company remuneration reports). For a chart enumerating S&P and ASX 300 with a first strike on their 2011 remuneration report, see DANIEL J. SMITH & MICHAEL CHANDLER, ISS, 2012 VOTING SEASON PREVIEW: AUSTRALIA AND NEW ZEALAND (2012), *available at* http://www.issgovernance.com/files/private/AustraliaNZPreview2012.pdf.

132. *See Australian Shareholders to Get More Say on Pay*, BUS. INSIDER (Mar. 3, 2011), http://articles.businessinsider.com/2011-03-03/markets/30035966_1_shareholders-remuneration-responsible-investor.

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believing the rule should be scrapped entirely.[133] Similarly, the Sydney-based law firm Mallesons Stephen Jaques publicly renounced the effectiveness of the Two-Strike Rule in an annual publication based on its experience and November 2011 client director surveys.[134] The firm summarizes the common critique of the reform stating:

> The reforms appear to have drawn the attention of boards away from matters of greater strategic value to organizations and have largely been used as a punitive mechanism by disgruntled shareholders frustrated by challenging market conditions, rather than as a means of communicating shareholders' assessments of executive remuneration. In the words of one survey respondent, *"the reforms . . . only add compliance costs and provide a larger voice to activist minority shareholders."*[135]

On the other side of the issue, a 2012 Melbourne Institute and Global Proxy Solicitation study indicates 53.2% of shareholders report being "[m]ore . . . likely to vote against" a remuneration report this year if their company received a first strike at the 2011 AGM.[136] The same study shows 68.4% of shareholders report being more likely to vote against the board's re-election following its second strike.[137]

In 2012, Australian companies and executives have forgone bonuses, raises, and incentive compensation perhaps due in some part to weak shareholder returns and fear of the Two-Strike Rule.[138] Several Australian

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133. ALLENS LINKLATERS, ALLENS LISTED CLIENT SURVEY: CAMAC REVIEW OF ANNUAL GENERAL MEETINGS 2 (2012), http://www.allens.com.au/pubs/pdf/CAMACAllensListedClientSurvey Report.pdf *archived at* http://perma.cc/63NY-5REF; *see also* Matt Orsagh, *supra* note 129 (citing Susannah Moran, *Call to Overhaul AGMs Puts 'Two Strikes' Rule on Remuneration in the Firing Line*, AUSTRALIAN (Aug. 8, 2012), http://www.theaustralian.com.au/business/companies/call-to-overhaul-agms-puts-two-strikes-rule-related-to-remuneration-in-the-firing-line/story-fn91v9q3-122 6445141935 (subscription required)). For a specific articulation of management's disapproval of the Two-Strike Rule (and other provisions) see the IAG's submission in opposition of the Treasury's Exposure Draft Bill, *available at* http://iag.com.au/news/gov_submissions/docs/20110309_SUB.pdf; and Kym Sheehan's similarly submitted opposition, *available at* http://docsfiles.com/pdf_submission_to_exposure_draft_corporations_amendment_further.html.

134. MALLESONS, *supra* note 131, at 1.

135. *Id.* at 13 (alteration in original).

136. UNIV. OF MELBOURNE, FACULTY OF BUS. & ECON., THE GLOBAL PROXY—MELBOURNE INSTITUTE SHAREHOLDER CONFIDENCE INDEX 3 (2012), http://www.melbourneinstitute.com/downloads/macro/2012/GPS/GPS_MI_Report_Aug2012.pd; *see also* SMITH & CHANDLER, *supra* note 131, at 3.

137. *Id.*

138. Matt Orsagh, *supra* note 129 (citing Matt Orsagh, *Corporate Governance Roundup*, CFA INSTITUTE (Aug. 31, 2012), http://blogs.cfainstitute.org/marketintegrity/2012/08/31/corporate-governance-roundup-aussie-bosses-give-back-turkeys-new-code-manu-a-bad-investment-director-defenestration-in-u-s/, *archived at* http://perma.cc/JW5B-DJ34); *see also* SMITH & CHANDLER, *supra* note 131, at 6;

companies have already promised to restrain pay policies even despite their rising earnings,[139] in what some have called "high-profile displays of remuneration 'austerity.'"[140] Other CEOs and boards have enforced cuts and freezes to fixed salaries for top executives.[141] The ISS claims these actions show "a burgeoning trend amongst some captains of industry to blunt allegations of runaway executive remuneration."[142] One recent academic study finds that in the first year of the "two strike" rule "CEO pay changes were negatively related to the level of shareholder dissent on the remuneration report," but that shareholders may have been too harsh on firms.[143] In the second year, however, the authors find that this trend was mitigated, especially for firms that received their second strike.

D. Belgium

1. Regulatory Framework for Shareholder Approval of Executive Remuneration Arrangements

The Belgian legal rules relating to compensation are straightforward: the company's articles of association (or, if they are silent, the general meeting of shareholders) determine both whether the directors shall be remunerated[144] and, if they are to be paid, the remuneration package for the services as board member.[145] Alternatively, the shareholders at the general meeting could indirectly decide to pay the directors by approving the company's accounts in which the remuneration is included (as a cost).[146] The general meeting of shareholders' decision about the remuneration of the directors only relates to the total amount granted to

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Jane Wardell, *Australian CEOs Sacrifice Bonuses, Wary of Powerful Shareholders*, TRUST.ORG (Aug. 23, 2012), http://www.trust.org/trustmedia/news/australian-ceos-sacrifice-bonuses-wary-of-powerful-shareholders/ (discussing Australian CEOs forgoing bonuses).

139. Matt Orsagh, *supra* note 129 (noting announcements by ANZ Bank CEO Mike Smith and Commonwealth Bank CEO Ian Narev).

140. SMITH & CHANDLER, *supra* note 131, at 6.

141. *Id.*

142. *Id.* at 7.

143. Reza Monem & Chew Ng, *Australia's 'Two-Strikes' Rule and Pay-Performance Link: Are Shareholders Judicious?*, 9 J. CONTEMP. ACCT. & ECON. 237, 238 (2013), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2334285.

144. The Belgian director can be remunerated, but does not have to be. CODE DES SOCIETES [C.SOC] [COMPANIES CODE] art. 517 (Belg.).

145. D. Willermain, *Le statut de l'administrateur de sociétés anonymes: principes, questions et réflexions*, 2008 REVUE DES SOCIÉTÉS 207, 236.

146. *Id.* at 236 n.95.

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the board of directors. The board of directors decides how this total compensation package will be divided between the directors.[147]

In 2002, the statutory creation of a modified two-tier board structure in the Belgian Companies Code affected the director remuneration rules.[148] Firms have the option through their articles of association to empower the board of directors to delegate a large part of its powers to a management committee. In the event that the company's articles of association do not to provide rules for setting the compensation of the management committee members, the board of directors is empowered to set the remuneration package.[149] The board of directors has the power to set the pay of the corporate senior officers, such as the members of the management board and/or officers empowered to execute the day-to-day management of the company. The duties of the executive board members are therefore split between board membership and providing their services as executives.

Shareholders' powers to determine executive compensation at Belgian companies were increased after the financial crisis and the national and international debates regarding excessive remuneration of top executives. The law of April 6, 2010 altered the corporate governance rules for executive pay for listed and state-owned companies.[150] As a result, in their annual reports Belgian firms must now include a corporate governance statement,[151] as well as a detailed remuneration report. Moreover, they must establish a remuneration committee, set criteria for the variable part of the executive remuneration and have generous golden parachutes approved by the shareholders.

In addition, the general meeting of shareholders must every year vote on the company's remuneration report, a "Say on Pay" vote. According to the Companies Act, the remuneration report must provide detailed information on eleven remuneration items: (i) the process the board used in developing the remuneration policy, (ii) a statement of how the directors applied the remuneration policy during the accounting period, (iii) the remuneration package of each individual non-executive board member, (iv) the remuneration that senior executive officers receive for their role as directors, (v) the criteria and procedure to grant performance related pay to executive board members and senior executive officers,

147. *Id.* at 237.

148. Law of Aug. 2, 2002, Moniteur Belge [M.B.] [Official Gazette of Belgium], Aug. 22, 2002, 36555 (Belg.).

149. C.SOC art. 524 (Belg.).

150. Law of April 6, 2010, M.B., April 23, 2010, 22709 (Belg.).

151. Council Directive 78/660, art. 46a, 1978 O.J. (L222) 27 (EC), on the annual accounts of certain types of companies, inserted by Council Directive 2006/46, 2006 O.J. (L 224) 1 (EU).

(vi)a detailed description of the individual remuneration package of the chief executive officer, (vii) a detailed description of the global remuneration package of the other senior executive officers, (viii) the number and main characteristics of shares, options and other rights granted, vested and/or executed, (ix) severance pay commitments, (x) the applied severance pay in case an executive board member or senior executive officer departed, and (xi) claw back provisions for variable pay based on misleading financial information.[152]

The shareholder vote is advisory so that the company is not obliged to revise any contractual engagements. Nor does the disapproval of the remuneration report affect the validity of the company's financial statements. However, if the shareholders disapprove the remuneration report, the board of directors is likely to revise the company's remuneration policy.[153]

The law of April 6, 2010 amended the Belgian Companies Code to give shareholders further power to restrict the structuring of the variable remuneration package and the share-based remuneration of the executives. It now requires a shareholder vote, or a facilitating article of association,[154] if the remuneration package of an executive board member or a senior executive provides for variable remuneration of which more than half is based on performance criteria of one year or less, or grants more than one quarter of the variable remuneration based on performance criteria measured over less than two years, or awards more than one quarter of the variable remuneration based on performance criteria measured over less than three years.[155]

Furthermore, the Belgian Companies Code now also requires shareholder approval, or a facilitating article of association, to deviate from a minimum "vesting period" for shares and share-based remuneration. Shares must not be vested earlier than three years after they are granted, while share options or other share-based benefits must not be exercisable earlier than three years after they are granted.[156] Finally,

152. C.SOC art. 96, § 3 (Belg.).

153. Belgian House of Representatives, 2336/001, at 18 (Dec. 22, 2009).

154. For which the general meeting of shareholders need to provide in the amendment of the articles of association.

155. C.SOC art. 520ter (Belg.). This provision is not applicable if the variable part of the remuneration is less than 25 percent of the total remuneration. *Id.*

156. CODE DES SOCIETES [C.SOC] art. 520ter, § 1 (Belg.). This provision is not applicable in case the variable part of the remuneration is less than 25 percent of the total remuneration. For an overview and analysis, see Hans De Wulf, Christoph Van der Elst & S. Vermeesch, 2010 *Radicalisering van corporate governanceregelgeving: remuneratie en transparantie na de wet van 6 april 2010*, TIJDSCHRIFT VOOR BELGISCH HANDELSRECHT 909–62.

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severance pay arrangements with executive directors and senior executive officers that exceed the amount of 12 months[157] remuneration[158] require the pre-approval of the general meeting of shareholders.[159]

2. *Assessment of Shareholder Voting Power on Executive Remuneration Agreements in Belgium*

The new Belgian Corporate Governance Code, with both a mandatory "Comply or Explain" requirement and a mandatory requirement to provide a remuneration report, greatly increased the amount of information disclosed concerning the remuneration of directors and executives and corporate remuneration practices. Previously most corporate boards did little to insure that shareholders had much say on executive remuneration policies. For example, in 2011, the last year before the new Say on Pay law came into operation, only 40% of the companies had the total gross remuneration package of the board of directors, or of a newly elected director, explicitly approved by the general shareholder meeting. The remaining companies had the directors' pay automatically approved with the approval of the financial statements.

In 2012, once the new Say on Pay law went into effect, over 90% of the companies put the item "remuneration report" on the agenda of the general meeting of shareholders.[160] Once again, companies' remuneration reports received high approval ratings from shareholders, although lower on average than in 2011. In Bel 20 companies,[161] the mean approval rate for companies' remuneration reports was 90.6%. A broader set of companies showed an even higher approval rate of 95.3%. In both instances, the median approval rates were even higher.

However, these figures conceal some companies where shareholder opposition was significant. For example, the shareholders of Agfa approved the company's remuneration report by a bare minimum with

157. In legal doctrine, it is debated whether the legislation requires the approval of the general meeting of shareholder from twelve months onwards, Wulf, Van der Elst & Vermeesch, *supra* note 156, at 946, or from eighteen months onwards, M. Wyckaert & T. Boedts, *Remuneratie van 'leiders' van genoteerde vennootschappen na de wet van 6 april 2010*, 5 TIJDSCHRIFT ESTATE PLANNING 291, 306 (2010).

158. The Dutch wording in the law is "wage."

159. The *next* general meeting of shareholders must *pre*-approve this severance pay arrangement. The arrangement is null and void in case this procedure is not applied.

160. The other companies did not comply with the law (Christoph Van der Elst, *Shareholders as Stewards: Evidence from Belgian General Meetings* 16 (Fin. Law Inst., Univ. of Ghent, Working Paper No. 2013-05, 2013), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2270938.

161. Bel 20 is an index of the twenty Belgian blue chip stocks. *Bel 20*, EURONEXT (last updated Jan. 30, 2015), https://indices.euronext.com/ en/products/indices/BE0389555039-XBRU.

only 50.3% of the votes cast in favor, while the AGM of EVS approved its report with 64%, and only 69% of the Delhaize shareholders approved its report.[162] Importantly, all three companies have a relatively dispersed-ownership structure, and the other agenda items for the AGM, including the remuneration of the board members, were overwhelmingly approved.[163] Nevertheless, these votes clearly signaled discontent amongst these firms' shareholders with the board's remuneration policy.[164] At the 2013 general meeting of the government controlled telecom operator Belgacom the shareholders disapproved the remuneration report. The government held a large stake and withheld its votes, while over 70% of the remaining shareholders[165] voted against the report because it contained overly generous remuneration packages for the managers and directors.[166] Later that year, the CEO was dismissed and replaced.[167] The new CEO had to agree with a salary of maximum €650,000, less than half of the remuneration package of the previous CEO.[168] In 2014 the remuneration report of Belgacom was approved, although the government still abstained.[169]

In 2014 some other companies, like Agfa Gevaert and Arseus, experienced at the AGM a no vote for their remuneration report. Both companies started up discussions with shareholders to find out what triggered the investors to vote against the remuneration report.[170]

A remuneration report highlights many features of executive remuneration that can deviate from the proxy advisors,' as well as many investors,' positions. These can lead to the Pensions Investment Research

162. Van der Elst, *supra* note 160, at 15.

163. *Id.* at 16.

164. *Id.*

165. Only 5% of the attending shareholders supported the remuneration report.

166. The minutes of the meeting are available at http://www.belgacom.com/assets/content/mbimport/%7B6B2D2E46-9049-46DA-8C21-1BB1DCAF3C1A%7D?transformationID=CustomContent&contentType=content/custom&previewSite=cow (last visited May 3, 2013), *archived at* http://perma.cc/GB8Y-F3A3.

167. Temmerman, *Labille: Belgacom is back to business*, DE STANDAARD (Nov. 15, 2013, 21:21 PM), http://www.standaard.be/cnt/dmf20131115_00839834.

168. Van Belle, *Akkoord over nieuwe CEO Belgacom*, DE STANDAARD (Jan. 8, 2014, 12:52 PM), http://www.standaard.be/cnt/dmf20140108_00918105.

169. The minutes of the meeting are available at http://www.belgacom.com/assets/content/mbimport/%7B4685B5C8-7E07-486D-A94F-7AD0F9AC23E3%7D?transformationID=CustomContent&contentType=content/custom&previewSite=cow (last visited August 20, 2014), *archived at* http://perma.cc/6E9C-PH88.

170. Stefaan Michielsen, *Aandeelhoudersstem vervliegt in de wind*, DE TIJD (May 17, 2014, 0:00 AM), *available at* http://www.tijd.be/nieuws/archief/Aandeelhoudersstem_vervliegt_in_de_wind.9502933-1615.art?highlight=aandeelhoudersstem%20vervliegt.

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Consultants (PIRC),[171] ISS and ECGS opposing, or issuing an "abstain vote" recommendation on, the company's remuneration report. Many investment managers follow these recommendations.[172] This is the likely explanation of the significantly higher shareholder opposition for the remuneration report, and in case of a company with a more dispersed shareholder structure, of even a majority no vote, like Agfa Gevaert and Arseus recently experienced. However, as many Belgian companies are blockholder controlled, and these blockholders support management, institutional investors' opposition does not lead to too big of a drop in overall shareholder support levels.

E. France

1. Regulatory Framework for Shareholder Approval of Executive Remuneration Arrangements

French public limited liability companies ("sociétés anonymes") are free to choose between a one-tier board structure and a two-tier board structure in the articles of association. A large majority of the companies adopt the one-tier board structure. The French commercial code requires the one-tier board of directors to elect a chairman,[173] either separating or combining this position with that of the chief executive officer.[174]

The French commercial code empowers the general meeting of shareholders to approve the total annual directors' fees for a one-tier board and the total annual supervisory board fees for a two-tier board.[175] This amount is paid for their services as board members[176] and not as executive officers. The shareholders must approve these payments, or the directors cannot be remunerated. The company can also provide directors with

171. PIRC is an independent research and advisory consultancy. For more information, see http://www.pirc.co.uk/.

172. Recent research shows that investment funds vote in line with the ISS recommendation in 69.35 per cent of the agenda items: Dragana Cvijanović, Amil Dasgupta & Konstantinos E. Zachariadis, *Ties that Bind: How Business Connections Affect Mutual Fund Activism* (ECGI Finance Working Paper No. 438/2014), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2317212.

173. CODE DE COMMERCE [C. COM.] art. L 225-47 (Fr.).

174. C. COM. art. L 225-51-1 (Fr.). This option is provided to the board in 2001. Loi 2001-420 du 15 mai 2001 sur les Nouvelles Régulations Economiques [Law 2001-420 of May 15, 2001 on the New Economic Regulations], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], May 16, 2001, p. 7776.

175. C. COM. art. L 225-47, 225-83 (Fr.).

176. This is the "attendance" fee for meetings of the board of directors.

travel allowances and reimburse their business expenses[177] and pay directors additional amounts for performing specific duties.[178] While the shareholders approve the total amount of director compensation, only the board of directors, or the supervisory board at a two-tier board company, can allocate specific amounts of compensation to the individual directors.

For many years, the shareholders' only power with respect to director pay was their approval over the total remuneration for the board. More recently, beginning in 1995, the French legislature has focused on the transparency of the remuneration package of directors and executives; however, it has not empowered the shareholders to have a "Say on Pay."[179]

Instead, initially in 2005, and subsequently reinforced in 2007, French law provides that the general meeting of shareholders must approve two parts of a "common" remuneration package of executive directors and officers: termination agreements and additional retirement agreements.[180] The 2005 Breton Law[181] determined that for these two types of payment, any agreements entered into are subject to the same strict approval requirements as those applied to related party transactions.[182] These strictly regulated agreements are only valid if they get prior approval by the Board, the chairman of the board sends a notice to the auditors, the auditors issue a report, and the general meeting of shareholders approves them.[183] Directors of companies that "failed or directors who have personally failed" cannot receive any kind of termination fee.[184] Under the

177. C. COM. art. R 225-33 (Fr.).

178. Board members can enter into employment agreements with the company.

179. Ivan Tchotourian, *Une décennie d'excès des dirigeants en matière de rémunération. Repenser la répartition des pouvoirs dans l'entreprise: une solution per se porteuse de risques*, *in* RISQUES D'ENTREPRISES: QUELLE STRATÉGIE JURIDIQUE? 44–48 (L. Nurit-Pontier & S. Rousseau eds., 2011).

180. Press Release, AMF, Fiche presse: Les remunerations des dirigeants 2 (Dec. 8, 2009), *available at* http://www.amf-france.org/documents/general/9219_1.pdf. The French corporate governance code forbids termination agreements from awarding more than two years of the sum of fixed and variable remuneration.

181. Loi 2005-842 du 26 juillet 2005 pour la confiance et la modernisation de l'économie [Law 2005-842 of July 26, 2005 on the Trust and Modernization of the Economy], J.O., July 27, 2005, p. 12160.

182. These are defined to include agreements between the company and its CEO, one of its Managing Directors, one of its directors, a shareholder holding a fraction of the voting rights in excess of 10% or the controlling company entered into directly or through an intermediary. C. COM. art. L 225-38 (Fr.). This is the authorized agreements and commitments provision.

183. These approvals are required every time the agreement is renewed.

184. ASSOCIATION FRANÇAISE DES ENTREPRISES PRIVÉES, CORPORATE GOVERNANCE CODE OF LISTED CORPORATIONS at 27 (Apr. 2010), *available at* http://www.afep.com/uploads/medias/documents/Code_gouvernement_entreprise_societes_cotees_Juin_2013_en.pdf. The Code does not provide much guidance as to what is considered as a personal failure of the director ("des dirigeants qui sont eux-mêmes en situation d'échec"). *Id.* The Code indicates the "demanding" (individual)

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2005 law, shareholders can reject termination agreements and additional retirement benefits. However, the remaining pieces of an executive's remuneration package are not subject to shareholder approval.[185]

French company shareholders do have some indirect influence over some elements of executive compensation packages. For example, the French commercial code requires that the shareholders vote to give the board the power to grant (free) restricted stock[186] and stock options[187] to the employees and the executive directors.[188] There are also some additional disclosure requirements. Under the 2007 TEPA Law,[189] the board of directors must disclose to the shareholders two reports related to any termination agreement: one that describes how the directors determined the performance conditions and the second detailing how those conditions are achieved.[190]

Like other countries, France has a mandatory "Comply or Explain" corporate governance code, called the AFEP-Medef Corporate Governance Code of Listed Corporations ("French Corporate Governance Code"). Companies in France are free to adopt this code's principles, but are not required to do so if they explain why they do not comply.[191] This code emphasizes the importance of full disclosure of the remuneration packages of the executive officers and board members.

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performance requirements must have been met unless the departure is due to a change of control or change in strategy. *Id.*

185. C. COM. art. L 225-40 (Fr.).

186. C. COM. art. L 225-197-1 (Fr.). The provision was inserted by Loi 2004-1484 du 30 décembre 2004 de finances pour 2005 [Law 2004-1484 of December 30, 2004 Relating to the Financing 2005], J.O.R.F., Dec. 31, 2004, art. 83, p. 22459.

187. The procedure for granting stock options was already introduced in the late 1980s. C. COM. art. 225-186-1 (Fr.) (*introduced by* Loi 87-416 du 17 juin 1987 sur l'épargne [Law 87-416 of June 17, 1987 on Savings], J.O., June 18, 1987, art. 19).

188. The persons to whom the restricted stock and options can be granted are the chairman of the board of directors, the chief executive officer, the executive members of the board and the management board members in a two tier board structure.

189. Loi 2007-1223 du 21 août 2007 en faveur du travail, de l'emploi et du pouvoir d'achat [Law 2007-1223 of August 21, 2007 to Support Work, Employment and Purchasing Power], J.O., Aug. 22, 2007, p. 13945.

190. Loi 2008-448 du 7 mai 2008 pris pour l'application des articles L. 225-42-1 and L. 225-90-1 du code de commerce et relatif à la publicité des rémunérations différées [Law 2008-448 of May 7, 2008 Regarding the Application of the Articles L. 225-42-1 and L. 225-90-1 of the Commercial Code and Related to the Publication of the Deferred Remuneration], J.O., May 11, 2008, p. 7831. The board of directors must also submit a specific resolution relating to severance pay arrangements for the approval of the general meeting of shareholders. *Id.*

191. Gerard Charreaux & Peter Wirtz, *Corporate Governance in France* 3 (Université de Bourgogne Working Paper no. 1070201, 2007), *available at* http://www.virtusinterpress.org/additional_files/book_corp_govern/sample_chapter04.pdf.

In June 2013, the French Corporate Governance Code introduced a "Say on Pay" vote for shareholders with companies choosing either to comply by providing the vote or to explain why they did not do so. Companies that comply are required by Principle 24.3 "to present"[192] to the general meeting of shareholders for an advisory vote the individual remuneration packages of the executive directors (i.e. the corporate officers). They must disclose both fixed and variable compensation on an annual and, where necessary, multi-year basis. The disclosures must state any exceptional remuneration, share options, performance shares or other long-term pay for performance, golden parachutes, retirement benefits and in-kind benefits.

Shareholders vote separately on the remuneration package of the CEO and the other executive board members. If the shareholders vote against the pay packages (called providing "a negative advice"), the board of directors must, at one of its next meetings and after being advised by the remuneration committee, "deliberate" about the implications of the shareholder vote. Upon concluding these deliberations, the board must publish on the company's website the actions it intends to take, if any, in response to the shareholders' concerns.[193]

Enactment of the Comply or Explain principle in the French Corporate Governance Code avoided—at least temporarily—the introduction of a statutory "Say on Pay" requirement. According to Reuters, the government supports the Comply or Explain rule.[194] However, the French government introduced a new tax regime for the "rich," indirectly addressing what they consider excessive remuneration packages.[195] Furthermore, at state-controlled enterprises, including (large) listed companies like EDF and Aeroports de Paris, the government has mandated limits on the remuneration of the members of the board of directors to €450,000.[196] Clearly there is more to come for executive pay regulation in France.

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192. At the time of this writing, the English version of the Code was not yet available.

193. Association Française des Entreprises Privées, *supra* note 184, at 32.

194. Leila Abboud, *Ad Agency Publicis Brings Say on Pay to France*, REUTERS, (May 29, 2013, 2:08 AM) http://uk.reuters.com/article/2013/05/29/publicis-pay-idUKL5N0EA2AG20130529?feedType=RSS&feedName=rbssFinancialServicesAndRealEstateNews. We presume that the new edition of the French corporate governance code with "say on pay" convinced the French government that—at the moment—no legislative action is required and that the mandatory Comply or Explain regime of the code with respect to provide in a say on pay of individual director's remuneration is sufficient.

195. French law now imposes a tax of 75% that companies have to pay for the remuneration packages passing €1 million. Loi 2013-1278 du 29 décembre 2013 de finances pour 2014 [Law 2013-1278 of December 29, 2013 on the financing of 2014], J.O., Dec. 30, 2013, p. 21829 *available at* http://www.legifrance.gouv.fr.

196. Loi 2012-915 du 26 juillet 2012 relatif au contrôle de l'Etat sur les rémunérations des dirigeants d'entreprises publiques [Decree 2012-915 of July 26, 2012 on the Government Control of

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2. *Assessment of Shareholder Voting Power on Executive Remuneration Agreements in France*

In this Part, we pull together heretofore-uncompiled primary data to assess the shareholders' voting power on executive compensation arrangements at French companies.[197]

a. *Voting on Total Board Pay*

As discussed above, the shareholders vote to authorize directors' fees for French corporations.[198] However, companies only need to hold such a vote if they seek to increase these fees. Our analysis of the CAC-40[199] companies' minutes from their general meetings from 2010 to 2012 shows that 53% of these companies sought shareholders' approval of directors' fees once during these three years.[200] More frequent approval was quite unusual: just three companies put the item on the agenda twice, and only two companies sought approval three times. Figure 1 below illustrates these data. We also note that one out of every three companies did not seek shareholder approval of these fees during these three years.[201]

Overall, and consistent with other countries, there is no significant opposition against the remuneration of French board members. Only three boards experienced opposition of more than 5% of the votes, with highest dissenting vote (almost 20%) at Société Générale in 2011.[202] According to ISS research, in 2010 and 2011, the shareholders approved the

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the Remuneration of the Directors of Government Controlled Companies], J.O., July 27, 2012, p. 12283.

197. Institutional Shareholder Service (ISS) and Association Française de Gestion Financière (AFG) provide in a general overview of voting issues. ISS, *2012 Proxy Season Review: World Markets*, at 15–25, http://www.issgovernance.com/files/private/2012CombinedPostseasonReport.pdf (last visited July 15, 2013); AFG, *Exercice des droits de vote par les sociétés de gestion en 2012*, at 16 (Mar. 2013).

198. M. COZIAN, A. VIANDIER & F. DEBOISSY, DROIT DES SOCIÉTÉS 303, nr. 541 (2012).

199. 38 large companies are in the sample. One company is registered in Belgium, the other in the Netherlands. Those two companies were excluded from the list.

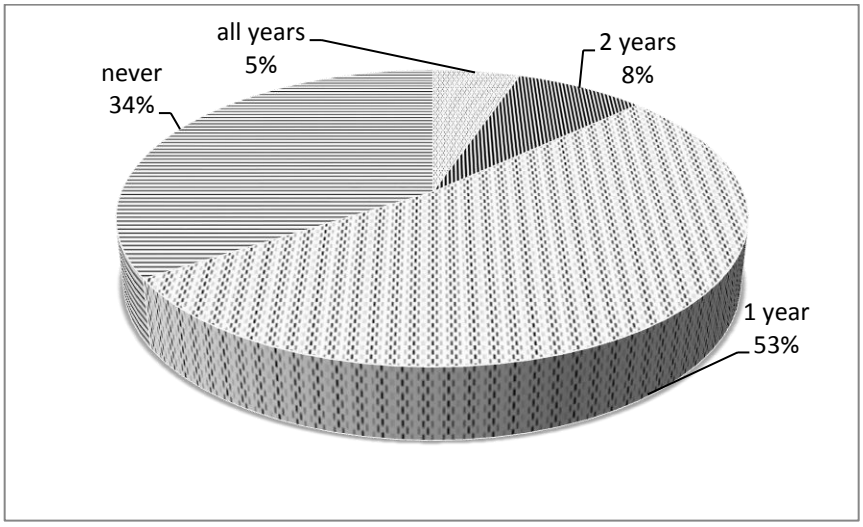
200. Only one AGM approved the fee in 2012, in all other cases the approval was equally split between the AGM 2010 and the AGM 2011.

201. Some companies do not change the board fee for even longer periods and hence do not ask for any shareholder approval. The latest say on board pay of Saint Gobain was in 2006 and the latest of Total was in 2007. The fee of the board of Vivendi remained unchanged between 2000 and 2008, of Lafarge between 2001 and 2010, of LVMH between (at least) 2004 and 2012, and at L'Oreal between 2005 and 2011.

202. This disapproval rate already dropped from 27% in 2009.

remuneration of the directors with 98.4% and 97.3%, respectively.[203] The approval rates of 2012 do not differ significantly from those of earlier years.[204]

FIGURE 1: APPROVAL OF THE TOTAL BOARD ATTENDANCE FEE AT CAC-40 COMPANIES' AGMS 2010–2012



b. Strength of Shareholder Voting on Other Elements of Executive Pay

ISS data shows an increase in the numbers of shareholders voting on executive remuneration elements at French general meetings.[205] In particular, they find that votes that are directly or indirectly related to compensation, like the vote to authorize the board to grant restricted stock to employees and executive directors, and the vote to authorize termination agreements, can run into significant opposition.

203. INSTITUTIONAL S'HOLDER SERVS., 2010 VOTING RESULTS REPORT EUROPE 23, tbl.12 (Sept. 16, 2010); INSTITUTIONAL S'HOLDER SERVS., 2011 VOTING RESULTS REPORT EUROPE 16, tbl.12 (Sept. 12, 2011).

204. Authors' calculations based on the minutes for the meetings of CAC-40 companies (on file with authors).

205. ISS noted an increase in the attendance rates from 64.5% in 2008 to 68.8% in 2011 for France.

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One measure of shareholder views on executive compensation is how they vote on share incentive plans. In 2010, ISS found that the mean shareholder dissent rate for these plans was 14.2%, which dropped to 12.5% in 2011.[206] In both years, approximately 10% of these plans were rejected by shareholders.[207] We note that France is the only Continental European country where these plans are regularly disapproved. However, it is unclear why shareholders fiercely oppose these particular stock plans. One plausible explanation could be that the board of directors is viewed as being given too much discretionary power in the plans: the board sets the performance conditions, selects the beneficiaries, and chooses the allotment terms, etc.[208]

For 2012, we collected data on shareholder voting for all agenda items of CAC-40 companies and selected remuneration related agenda items: severance payment arrangements, authorization of the board to allot restricted stock, and authorization of the board to grant stock options on shares and retirement plans. The results are summarized in Table 1 below.

TABLE 1: AGENDA ITEMS OF GENERAL MEETINGS 2012 OF CAC-40 COMPANIES RELATED TO REMUNERATION[209]

	Number of items voted on	Number of companies holding votes	Mean shareholder approval rate	Remarks on Outcome of Voting by Shareholders
Termination agreement	16	11 (29%)	66.60%	1 rejected
Restricted stock	14	13 (34%)	83.81%	1 rejected/1 withdrawn
Share options	4	4 (11%)	92.26%	
Retirement plan	3	3 (8%)	80.37%	1 rejected

Table 1 shows that termination agreements are an agenda item at 29% of the companies and that shareholder opposition to them is relatively high: the average approval rate was only 66.6%. Looking more carefully at

206. INSTITUTIONAL S'HOLDER SERVS., 2010 VOTING RESULTS REPORT EUROPE 23, tbl.12 (Sept. 16, 2010); INSTITUTIONAL S'HOLDER SERVS., 2011 VOTING RESULTS REPORT EUROPE 16, tbl.12 (Sept. 12, 2011).

207. *Id.*

208. *See, e.g.*, SANOFI, NOTICE OF GENERAL MEETING 2012, at 23 (2012), *available at* http://en.sanofi.com/Images/30146_2012_Avis_convocation_EN.pdf ("[The general meeting] resolves that the vesting of the shares will be subject to performance conditions which will be set by the Board of Directors concerning a period of at least three years.").

209. Based on thirty-eight of the companies in the CAC-40. Two CAC-40 companies, Solvay and EADS, have their registered seat outside of France, although they are listed on the French stock exchange. We have excluded these companies from the analysis as they are not subject to the French voting rules.

the data, we see that two thirds of the termination agreements received more than 25% shareholder opposition and that more than 40% of shareholders voted against seven such agreements. However, only the agreement of the CEO of Safran was disapproved. The shareholders also rejected the retirement plan of Safran's CEO, but the two other retirement plans were both approved by more than 98% of the votes.[210]

Stock option plans are generally considered as appropriate methods for incentivizing the executive board and management. Table 1 displays data illustrating that none of these plans garnered more than 15% opposition. Finally, shareholders were generally less enthusiastic about performance share plans. For example, the board of directors of France Telecom chose to withdraw this agenda item from the general meeting, while shareholders at other companies supported the authorization with less than 86% of the votes.

We also studied the compliance with the aforementioned new best practice principle 24.3 "to present" to the general meeting of shareholders for an advisory vote the individual remuneration packages of the executive directors (i.e. the corporate officers). All CAC-40 companies provided the shareholders with this advisory vote of the remuneration package of the CEO.[211] For other corporate officers we found mixed results. Some companies offered the shareholders the opportunity to vote on one or more executive directors, while others only provided the vote on the remuneration package of the CEO. However, the corporate structures of French groups differ significantly so it is not directly noticeable whether the company fully complied with the best practice 24.3 or not. The remuneration package of most CEOs was overwhelmingly approved, with 80% of the packages receiving more than 90% positive votes. None of the remuneration packages was disapproved. However the opposition was between 30% and 40% of the votes at three companies. It is too early to assess what triggers shareholders to vote against the remuneration package of the CEOs of the largest French companies. The total remuneration package can only be one of many other reasons. According to research published by Capital,[212] the CEOs of Sanofi, LVMH and L'Oreal all gained more than €8 million and shareholders approved these packages

210. The details of the voting results can be found at http://www.safran-group.com/IMG/pdf/Resultats_AGM_SAFRAN_31-05-2012.pdf (last visited Sept. 4, 2014)

211. Authors' own research related to the minutes of the 2014 meetings of all of the CAC-40 companies.

212. *Le palmarès 2014 des salaires des patrons*, CAPITAL.FR (Apr. 3, 2014), http://www.capital.fr/carriere-management/special-salaires/2014/le-palmares-2014-des-salaires-des-patrons-922673, *archived at* http://perma.cc/DH4F-EME8.

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with 98%, 82% and 94%, while the CEO of Safran, who took only €1.6 million home, had his fee opposed by more than 36% of all shareholders.

F. Germany

1. Regulatory Framework for Shareholder Approval of Executive Remuneration Arrangements

a. The Two-Tier Board Structure

The mandatory two-tier board model is a core feature of the German stock corporation: the management board is responsible for running the business,[213] while the supervisory board must supervise the management board. The supervisory board can also be asked to approve specific types of transactions.[214] Directors that sit on one board cannot also sit on the other board at the same company.[215] The management board must manage and represent the company jointly unless the articles provide otherwise.[216]

The supervisory board elects the members of the management board for a term of up to five years and also has the power to dismiss the board. Members of the management board can only be removed for cause, like breach of duty or a vote of no confidence of the shareholders.[217] The members of the supervisory board are elected for maximum terms of four years. The size of the supervisory board depends on the value of the company's capitalization.[218] Further, the composition of the supervisory board is determined in part by different co-determination requirements.

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213. Aktiengesetz [AktG] [Stock Corporation Act], Sept. 6, 1965, BGBL. I, as amended, § 76, para. 1. The management board is composed of at least one natural person with full legal capacity. If the capital of the company is more than €3 million, the management board must comprise at least two members unless the articles of association allows a management board of one member. *Id.* § 76, para. 2.

214. *Id.* § 11, para. 5.

215. *Id.* § 105, para. 1; Klaus J. Hopt & Patrick C. Leyens, *Board Models in Europe. Recent Developments of Internal Corporate Governance Structures in Germany, the United Kingdom, France, and Italy* 6 (ECGI Law Working Paper No. 18/2004, 2004), *available at* http://ssrn.com/abstract=487944.

216. AktG § 77, para. 1, § 78, para. 2.

217. *Id.* § 84, para. 3.

218. *Id.* § 95. The supervisory board must be composed of at least three members, all natural persons. The articles of association can provide for a higher number but the number must be divisible by three, unless the codetermination laws provide otherwise. The maximum number of supervisory board members depends on the share capital of the company. Capital up to €1.5 million allows for a board of nine members, capital of more than €1.5 million and up to €10 million allows for a board of fifteen members, and capital higher than €10 million allows for a board of up to twenty-one members.

b. Shareholder Approval Requirements for Executive Remuneration

As early as 1937, the German Stock Corporation Act required that the supervisory board had to make sure that the compensation of the management was reasonable, reflecting both the duties of the management board as well as the financial condition of the company.[219] The 1965 version of this Act confirmed this reasonableness requirement. However, case law on the assessment of the reasonableness of the remuneration is scarce.[220]

Under this regime, shareholders had no voting rights on executive pay as it was the supervisory board's responsibility to make this determination. The one exception was for share option schemes. The German Stock Corporation Act had very strict rules regarding the issuance of shares and share related instruments to protect the incumbent shareholders against dilution. Prior to 1998, share options for the management board were only legally possible with the issuance of convertible, or warrant, bonds which required the approval of a three-fourths majority vote of the shareholders at a general meeting where more than 50% of the capital of the company was represented.[221] In 1998, the Control and Transparency Act ("KonTraG") explicitly allowed the general shareholders meeting to authorize management to buy back stock to use in a stock option plan for members of the management board, significantly increasing the use of variable pay at German companies.

In 2009, the German Parliament enacted a new law, the Law on the Appropriateness of Director Compensation ("VorstAG"), which changed the executive remuneration system in Germany. The new law has three main features for listed companies of which one is for stock exchange listed companies, the general meeting of shareholders can be (but does not

219. Brigitte Haar, *Executive Compensation under German Corporate Law: Reasonableness, Managerial Incentives and Sustainability in Order to Enhance Optimal Contracting and to Limit Managerial Power*, *in* RESEARCH HANDBOOK ON EXECUTIVE PAY, *supra* note 2, at 486, 490.

220. The Regional Court of München stated in 2007 that the remuneration can be reasonable even if it is not in line with common practice. Landgericht München I [LG München] [Regional Court of Munich], Mar. 29, 2007, Case No. 5 HK O 12931/06 DIE AKTIENGESELLSCHAFT [AKTG 2007] 458, 2007.

221. For a detailed analysis of all the difficulties to issue share (option) schemes for the management board, see Theodor Baums, *Aktienoptionen für Vorstandsmitglieder*, *in* FESTSCHRIFT FÜR CARSTEN PETER CLAUSSEN 3–48 (Klaus-Peter Martens, Harm Peter Westerman & Wolfgang Zöllner eds., 1997).

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have to be) provided an advisory vote regarding the remuneration system of the management board.[222]

The German Corporate Governance Code copied these new requirements, providing an option for the shareholders to approve the remuneration system for management board directors, but also stating that the supervisory board must determine the total compensation of an individual member of the management board.[223]

For supervisory board members, the general meeting of shareholders, or the articles of association of the corporation, may set the amount of its members' compensation.[224] The supervisory board members' remuneration must be related to the duties of the supervisory board and the condition of the company. The German Corporation Act also provides as an option that supervisory board members can be paid a short-term bonus tied to the profits of the company.[225]

2. *Assessment of Shareholder Voting Power on Executive Remuneration Agreements in Germany*

a. *Executive Remuneration in Germany*

The development of the remuneration package of the German management board is relatively well mapped, partially due to the litigation after Vodafone's acquisition of Mannesmann in 2000 over an award of golden parachute severance agreements.

German executive compensation packages have grown substantially in the interim. From 2001 to 2012, the mean remuneration of an average member of the management board ("Vorstand") of the thirty largest German public companies listed on the DAX more than doubled from less than €1.2 million to more than €3.0 million.[226] As Figure 2 illustrates, this increase resembles a kinked curve. Between 2001 and 2007, remuneration packages jumped significantly. However, in 2008, during the Financial Crisis, the compensation of an average member of the Vorstand decreased

222. AktG § 120, para. 4. The law only facilitates that the company allows the general meeting to vote on the remuneration system of the management board, there is no mandatory requirement.

223. Deutsche Corporate Governance Kodex [DCGK] [German Corporate Governance Code] Feb. 26, 2002, BUNDESANZEIGER [BANZ.], as amended May 15, 2012, §§ 2.2.1, 4.2.2.

224. AktG § 113, para. 1. As neither the articles of association nor the general meeting foresee in a remuneration, the members of the supervisory board must provide the services for free. *Id.*

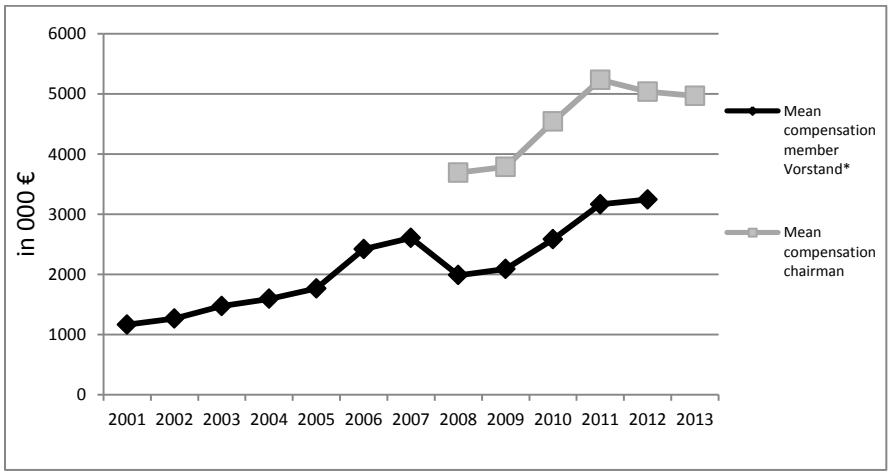
225. *Id.* § 113, para. 3.

226. *See* Figure 2 below.

by almost 30%. Since 2008, the Vorstand members' pay packages have increased again, surpassing their 2007 levels in 2011.

The CEO receives a much higher compensation than the other members. During this period, the mean compensation of the CEO soared from €3.7 million to over €5 million. At the highest end, the remuneration package of the CEO of Volkswagen reached €17.46 million in 2011.

FIGURE 2: EVOLUTION OF THE TOTAL REMUNERATION OF AN INDIVIDUAL MEMBER OF THE MANAGEMENT BOARD



* The remuneration does not take into account pension contribution. DEUTSCHE SCHUTZVEREINIGUNG FÜR WERTPAPIERBESITZ E.V.(DSW), STUDIE ZUR VERGÜTUNG DER VORSTÄNDE IN DEN DAX-UND MDAX-UNTERNEHMEN IM GESCHÄFTSJAHR 2010, sheet 7 (2011) (summarizing executive compensation for the years 2001–11), *available at* http://www.dsw-info.de/uploads/media/DSW_Verguetungsstudie_Vorstaende_2011_alle_Charts.pdf; DSW, STUDIE ZUR VERGÜTUNG DER VORSTÄNDE IN DEN DAX-UND MDAX-UNTERNEHMEN IM GESCHÄFTSJAHR 2012 sheets 2, 5 (2013) (summarizing executive compensation for the years 2011–12), *available at* http://www.dsw-info.de/uploads/media/DSW-Verguetungsstudie-2013-Tabellen.pdf, HOSTETTLER KRAMARSCH PARTNER, 2013 ERNEUT LEICHT RÜCKLÄUFIGE VORSTANDSVERGÜTUNG IM DAX, (Mar. 2014), *available at* http://www.hkp.com/cms/upload/media/DE/D_010_2014_hkp_PI_GB_ AuswertungVV_DAX_03_2014_final.pdf.

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b. Results of Shareholder Voting on Executive Remuneration[227]

While not mandatory,[228] all DAX companies have had their management board remuneration system approved at least once by their general meeting of shareholders since 2010. The general shareholders meetings at three firms, BMW, Beiersdorf and Munich Re approved the system every year between 2010 and 2012, even though the pay system of these companies was not changed in each of those years. Cite. Smaller companies are less keen to provide in a shareholder vote: in 2009 and 2010, 78% of the general meetings of M-DAX companies approved the remuneration system, only 42% of the meetings of S-DAX companies and 63% of the TecDAX companies did so.[229]

Over this time period, fewer companies have put their executives' pay practices up for a shareholder vote each year. Thus, while 90% of the DAX general meetings voted on the remuneration system in 2010, this dropped to 47% in 2011, and fell even further to 33% in 2012.[230]

At the same time, at DAX companies, the average shareholder approval rate for the compensation systems decreased between 2010 and 2012 from 91.6% to 89.9%. In the same vein, in 2010 and 2011, over 75% of compensation systems were approved by over 95% of company shareholders. However, by 2012, only 40% of companies' compensation systems were approved by more than 95% of the shareholder votes.[231]

In one important example, in 2010, the shareholders at Heidelberger Cement rejected the remuneration system of the company. Several other companies have experienced strong opposition to their proposed remuneration system, including Deutsche Bank in 2010 (42% opposed), [232]

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227. The data of this section are derived from the publication of DSW, DSW GRAFIKEN VERGUETUNGSVOTUM, 2011, *available at* http://www.dsw-info.de/fileadmin/downloads/Grafiken_Verguetungsvotum.pdf (last visited Jan. 25, 2013), and the authors' own research related to the minutes of the 2012 meetings of all of the DAX companies.

228. *See* Part I.F.1.b, *supra*.

229. The M-DAX, S-DAX and TecDAX are the indexes with fifty companies (M-DAX and S-DAX) or thirty companies (TecDAX) that are representative for the German mid-sized, small-sized and technology companies.

230. LG München, Mar. 29, 2007, Case No. 5 HK O 12931/06 [AKTG 2007] 458, 2007.

231. These data are based on calculations of the DSW reported approval rates for 2010 and 2011 DSW, STUDIE ZUR VERGÜTUNG DER VORSTÄNDE IN DEN DAX-UND MDAX-UNTERNEHMEN IM GESCHÄFTSJAHR 2010, 2011 sheet 11, *available at* http://www.dsw-info.de/uploads/media/DSW_Verguetungsstudie_Vorstaende_2011_alle_Charts.pdf); and authors' own research on all minutes of the 2012 meetings of DAX companies.

232. ISS argued that the opposition at Deutsche Bank was due to the significant increase of the base salary and would reduce the variable remuneration with the same amount but failed to specify any details on the target levels. INSTITUTIONAL S'HOLDER SERVS., 2010 VOTING RESULTS REPORT

Deutsche Börse (47% opposed) in 2010, Merck (30% opposed) in 2011 and SAP (35% opposed) in 2012.

As a result, Deutsche Bank, Heidelberg Cement and Merck resubmitted their remuneration systems for shareholder approval at subsequent general shareholder meetings. In response to Deutsche Bank's efforts to make its remuneration system more transparent (but only modestly changing the system itself)[233], its shareholders cast 94% of their votes in favor of the plan in 2012. Similarly, Heidelberg Cement developed a new remuneration system,[234] and over 96% of its shareholders approved the revised system in 2011. Ironically, Merck added a long-term variable compensation component[235] that actually increased the size of its executives' compensation, but its shareholders' support for the remuneration system went from 70% in 2011 to 87% in 2012.

Overall, the visible influence of German shareholders' votes on management remuneration systems is modest. Say on Pay is optional, though widely employed. When given the chance, shareholders generally approve of the remuneration systems and companies that experienced significant shareholder opposition against their remuneration system did not necessarily change their systems. There were more medium- and long-term incentive schemes,[236] resulting in more generous remuneration packages,[237] which are less transparent.[238] Whether the low levels of shareholder opposition are the result of companies having private consultations with major institutional investors, as reported in the financial press,[239] is not clear.

EUROPE25 (Sept. 16, 2010). Further, the annual report shows that the total remuneration of the management board increased from €4.5 million in 2008 to €39 million in 2009.

233. The 2012 general meeting notice of Deutsche Bank stated that the minor changes were due to new legal requirements (as a result of the transposed European Capital Requirement Directive III). *See* DEUTSCHE BANK, TAGESORDNUNG HAUPTVERSAMMLUNG 2012, at 4, *available at* https://www.deutsche-bank.de/ir/de/download/HV2012_Tagesordnung_de_2304.pdf).

234. It moved from a variable bonus based on a specific financial goal and a medium-term bonus towards a market competitive short-term bonus and a long term bonus. The short-term bonus is based on share of profit and individual targets as key performance indicators (KPI's). The long-term bonus is based for 50% on the three-year earnings before interest and tax (EBIT) and return on invested capital (ROIC) and for 50% on the four-year total shareholder return related to two indices.

235. Merck is organized as a limited partnership with a board of partners that has to approve the compensation system and which has delegated its power to a "personnel committee."

236. *See* AktG, Sept. 6, 1965, BGBL I, as amended, § 87, para. 1.

237. *See* DELOITTE, INFORMATIONEN FÜR AUFSICHTSRAT UND PRÜFUNGSAUSSCHUSS 2 (2012), *available at* http://www.deloitte.com/assets/Dcom-Germany/Local%20Assets/Documents/13_FocusOn/Center%20fuer%20Corporate%20Governance/2012/CGF%203-2012_safe.pdf.

238. Peter Wilke & Katrin Schmid, *Entwicklung der Vorstandsvergütung 2011 in den DAX-30-Unternehmen* 46 (Hans Böckler Stiftung Working Paper No. 269, 2012).

239. Steve Johnson, *Good Governance Delivers Good Value*, FIN. TIMES, Jan. 27, 2013, at 4. In

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In February 2013, in its latest proposed amendments to the corporate governance code, the German Corporate Governance Commission proposed that the supervisory board set a cap on the amount of total compensation awarded to individual management board members as well as a cap on the components of this remuneration.[240] Some commentators have suggested tying management pay growth to the level of increases in the employees' salaries.[241] The German government has also prepared a new proposal that will make Say on Pay binding for listed companies, but the German elections of September 2013 stopped the pending legislative procedure.[242]

G. Sweden

1. Regulatory Framework for Shareholder Approval of Executive Remuneration Agreements

Swedish public limited liability companies must have both a board of directors and a managing director. The board of directors must be comprised of three members or more.[243] More than half of the members of the board of directors must be elected by the general meeting of shareholders. The articles of association can provide for other bodies to elect the remaining directors, but this power cannot be delegated to the board of directors or one of its members.[244] Large listed Swedish companies commonly have all members of their board of directors elected by the shareholders.[245] In addition to the members elected by the general

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this interview with the head of corporate governance of Legal & General Investment Management, Sacha Sadan it is noted that many corporate governance issues are discussed with this institutional investor before the agenda of the general meeting is prepared.

240. GOV'T COMM'N OF THE GERMAN CORPORATE GOVERNANCE CODE, EXPLANATORY COMMENTS ON THE CHANGES PROPOSED BY THE CODE COMMISSION FROM THE PLENARY MEETINGS HELD ON 9 AND 31 JANUARY 2013, at 6 (Feb. 2013), *available at* http://www.dcgk.de/files/dcgk/usercontent/en/download/2013/konsultationsverfahren_2013_02_05/Explanatory_comments_on_the_changes_proposed_by_the_Code_Commission_from_the_plenary_meetings.pdf (last visited May 5, 2013).

241. Wilke & Schmid, *supra* note 238, at 45–46.

242. *Vernunft und Maß bei Managerbezahlung*, DIE BUNDESREGIERUNG (May 8, 2013), http://www.bundesregierung.de/Content/DE/Artikel/2013/05/2013-05-08-kabinett-aktiengesetz.html; *see generally* DEUTSCHER BUNDESTAG, Beschlussempfehlung und Bericht, June 26, 2013, BT 17/14214, *available at* http://dip21.bundestag.de/dip21/btd/17/142/1714214.pdf (last visited July 3, 2013).

243. 8 ch. 46 § AKTIEBOLAGSLAGEN [ABL] [THE SWEDISH COMPANIES ACT] (Svensk författningssamling [SFS] 2005:551).

244. *Id.* at 8 ch. 8 §.

245. A quick scan of the articles of association of Investor, Tele2, Telia Sonera, Volvo, Swedish Match, Electrolux, Securitas proves that none of these companies had other directors that were not

meeting of shareholders, the trade unions representing the firm's workers get to elect two or three directors to the board.[246]

The board of directors of public limited liability companies elects a managing director,[247] who is responsible for the day-to-day management of the firm under the guidance of the board of directors.[248] The managing director may also take extraordinary actions if they must be done so quickly that she cannot wait for a decision of the board of directors.[249]

The general meeting of shareholders determines the remuneration of the board of directors. Since 2006, unlike in France and Belgium, the general meeting of shareholders for Swedish companies sets individual director's fees separately,[250] although individual directors are generally paid about the same. Like in France and Belgium, the directors receive a fixed director's fee with an additional fee for committee work and a flat fee if they serve as chairman of the board.

In addition, since 2006, the general meeting of shareholders of Swedish listed companies casts a binding vote, a "Say on Pay" vote, for or against the board of directors' proposed remuneration guidelines for determining the remuneration of the managing director and the company's senior

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elected by the general meetings of shareholders or were not employee representatives. ELECTROLUX, ARTICLES OF ASSOCIATION OF AKTIEBOLAGET ELECTROLUX (COMPANY NO. 556009-4178) art. 6 (May 8, 2002), *archived at* http://perma.cc/5L5S-6HWR (English), http://perma.cc/7ZHN-GG77 (Swedish); INVESTOR, ARTICLES OF ASSOCIATION FOR INVESTOR AB (REG. NO. 556013-8298) § 5 (Apr. 17, 2012); SECURITAS, ARTICLES OF ASSOCIATION FOR SECURITAS AB WITH CORPORATE IDENTITY NUMBER 556302-7241 § 6 (Jan. 10, 2011); SWEDISH MATCH, ARTICLES OF ASSOCIATION SWEDISH MATCH AB (PUBL) CORPORATE REG NO: 556015-0756 § 6 (May 2, 2012), *archived at* http://perma.cc/9FWX-ANG2 (English), http://perma.cc/8K7C-L3BK (Swedish); TELE2, ARTICLES OF ASSOCIATION TELE2 AB REG. NO 556410-8917 (May 13, 2013), *archived at* http://perma.cc/3VLV-7DLZ (English), http://perma.cc/996J-5MDN (Swedish); TELIA SONERA, ARTICLES OF ASSOCIATION § 9 (Apr. 6, 2011), *archived at* http://perma.cc/C5R-JKKD; VOLVO, ARTICLES OF ASSOCIATION FOR AB VOLVO § 9 (Apr. 4, 2013).

246. The right to elect two directors is provided to the unions if the company (or group) employs twenty-five employees or more. If the group employs more than 1000 employees, the Unions can elect three directors. 4 § LAG OM STYRELSEREPRESENTATION FÖR DE PRIVATANSTÄLLDA [BOARD REPRESENTATION (PRIVATE SECTOR EMPLOYEES) ACT] (SFS 1987:1245).

247. OECD, BOARD PRACTICES: INCENTIVES AND GOVERNING RISKS 95 (2011), *available at* http://dx.doi.org/10.1787/9789264113534-en. In private companies a managing director is an optional feature. *See* 8 ch. 27 § ABL.

248. *Id.* at 8 ch. 29 §. According to the Swedish Companies Act the board must develop instructions dividing the allocation of power between the board of directors and the managing director. *Id.* at 8 ch. 7 §.

249. *Id.* at 8 ch. 29, 50 §§. Legal doctrine recognizes the difficulty of separating the powers of the board of directors and the managing director CARL HEMSTROM, CORPORATIONS AND PARTNERSHIPS IN SWEDEN 84 (2011).

250. 8 ch. 23(a) § ABL. The board of directors is not permitted to divide a lump sum fee. ROLF, SKOG & CATERINA FÄGER, THE SWEDISH COMPANIES ACT 63 (2007).

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management.[251] The general meeting of shareholders must vote annually on the guidelines to be applied in the current accounting period.

The Swedish Companies Act provides a number of rules regulating the content of the remuneration guidelines. First, the guidelines must be forward looking but limited to the period until the next general shareholders' meeting.[252] Salary and all other types of compensation must be addressed, including the granting and vesting of options and any future payment in securities. When the exact amount of the remuneration cannot be predetermined, the guidelines must contain information on the nature of the compensation as well as the estimated total cost to the company.[253] Further, the company has to disclose information on the remuneration that has been approved by the board but is not yet payable. Also, the guidelines can provide that the board of directors has the right to deviate from these guidelines in individual and specific circumstances.[254]

Conversely, the Companies Act indicates that when the compensation package requires the company to issue shares, convertibles or warrants for the members of the board, or the managing director, no further guidelines must be provided.[255] The Companies Act itself provides the shareholders the right to approve this type of issuance by a supermajority of 90% of the represented votes and shares.[256] The report of the board of directors must also provide information about the issuance, including the allotment of the shares.[257]

The Swedish Companies Act states that three weeks before the general shareholders meeting, the company's auditors must provide a report certifying that the company complied with the guidelines approved by the AGM at the prior general meeting.[258] If the auditors opine that the company did not comply, their report must provide the reasons thereof.

The Act provides little guidance about the appropriate level of detail that must be disclosed in the guidelines submitted to shareholders. However, some things can be inferred from the Swedish Corporate Governance Code. For example, the Code defines executive pay as: "(i) fixed salary or fee, (ii) variable remuneration, including share- and share-price-related incentive programs, (iii) pension schemes, and (iv)

251. 7 ch. 61 § ABL.
252. *Id.* at 8 ch. 51 §.
253. *Id.* at 8 ch. 52 §.
254. *Id.* at 8 ch. 53 §.
255. *Id.* at 8 ch. 51 §.
256. *Id.* at 16 ch. 2, 8 §.
257. *Id.* at 16 ch. 10 §.
258. *Id.* at 8 ch. 54 §.

http://openscholarship.wustl.edu/law_lawreview/vol92/iss3/7

other financial benefits."[259] The Corporate Governance Code requires the general meeting to approve every kind of allotment of shares to executives, executive share-price related incentive schemes, and urges the company to provide detailed information on these schemes.[260]

At public companies, the shareholders also have the right to vote on the issuance of shares, warrants or convertible instruments to the board of directors, the managing director or employees that involve the suspension of the preemption rights of the incumbent shareholders. Such plans require the approval of 90% of the votes at a shareholders' meeting where at least 90% of the shareholders are present.[261] This rule makes it difficult to use most share-based incentive schemes, although many companies make use of alternative mechanisms, like phantom stock.

There have been some efforts to reduce the level of shareholder input on executive remuneration. In 2009, a governmental inquiry recommended changing the mandatory "Say on Pay" requirements into a less intrusive regulatory comply-or-explain regime, but no action has been taken to implement this recommendation thus far.[262]

2. Assessment of "Say on Pay" in Sweden

CEO pay is considered moderate in Sweden. In 2005, the average CEO's pay was below $1 million, less than half of their American counterpart. The pay package was skewed towards salary, bonus and social security contributions, with long-term incentives providing less than 10% of the total remuneration package.[263] Since then, pay has increased, but a recent survey estimated the average pay of the CEO's at the twenty-three largest companies at around 13.5 million Swedish krona (SEK), or less than $2 million, of which only one-third consisted of a variable short- and long-term incentive pay.[264]

According to the OECD, several large, listed Swedish companies with substantial foreign share ownership have discussed remuneration issues

259. KOD FÜR BOLAGSSTYRNING [SWEDISH CORPORATE GOVERNANCE CODE] III:9, at 22 n.10.

260. *Id.* at III:9, at 24.

261. This rule was introduced because it was found that some issues were taken place in violation of the then applicable company law. HEMSTROM, *supra* note 249, at 41.

262. *See* Per Lekvall, *Say on Pay—Pro or Con Good Governance? Some Reflections Based on the Swedish Experience*, BOARDVIEW,Apr. 2012, at 47–50.

263. Randall S. Thomas, *International Executive Pay: Current Practices and Future Trends* 9–10 (Vanderbilt Univ. Law Sch., Working Paper No. 08-26, 2008).

264. OECD, BOARD PRACTICES: INCENTIVES AND GOVERNING RISKS, CORPORATE GOVERNANCE 100, *available at* http://dx.doi.org/10.1787/9789264113534-en.

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with these investors.[265] They found that many foreign investors did not want to be involved in the setting of the remuneration package of individual executives and therefore relied on proxy advisory firms for advice on how to vote their shares. In order to stimulate voter turnout and the approval of remuneration policies, Swedish companies have been urged to invite foreign investors to participate directly (for example through conference calls). Overall, it does not appear that Say on Pay led Swedish shareholders to become more actively engaged with their companies.[266]

We examined the remuneration packages of the board of directors, the managing director and the top executives of OMX Stockholm thirty companies over 2011 to 2012.[267] In 2011, the chairman of the board at these firms received an average payment of 1.784 million SEK[268] (with a median of 1.655 million SEK), with a minimum compensation of 227,000 SEK and a maximum of 5.454 million SEK.[269] The remaining members of the board of directors elected by the shareholders[270] were remunerated with a mean director's fee of 615,000 SEK (with a median of 587,000 SEK). One company paid 1.130 million SEK to each individual director, while the average director of one large bank only received 91,000 SEK.[271]

In 2011, the mean CEO remuneration package was 18.8 million SEK. These packages ranged from a maximum of 38.54 million SEK for the CEO of a medical technology company to a minimum of 1.751 million SEK for the CEO of an oil company.[272] On average, half of the remuneration package is the fixed wage (median 46%), while the short term bonus contributed less than 20% of the total pay (both mean and median). Average pension contributions are considerable with a mean of 21% of total pay and a median of 18.5%. Company disclosures do not split

265. *Id.* at 105–06.

266. *See id.* at 106, 109.

267. There are twenty-six companies in our sample. Nokia, ABB and Astra Zeneca are considered as foreign companies, Atlas Copco counts as two in the index (shares A and B). For these companies, the average number of board members is eleven with a mean of 8.9 directors elected by the shareholders and 2.1 directors elected by the employees.

268. The mean values include the additional remuneration for memberships and chairmanships of committees in the board.

269. The chairman of Skania is also senior executive of Volkswagen and is not remunerated for his chairmanship of Skania.

270. The chief executive officer who generally does not receive a remuneration as director is the sole exception.

271. Employee directors are not separately remunerated.

272. Authors' own research based on companies' annual reports and websites (May 2013) referred to *supra* note 267 (on file with authors).

the costs of long-term benefits, but the total amounts of long-term benefits vary between 0 SEK and 8 million SEK.

This data shows that in Sweden the cross-company differences in pay packages are relatively low in comparison with other countries. The absolute amounts are nearly as high as those paid in some other countries. Perhaps as a consequence, shareholder opposition to company's remuneration guidelines, or the individual remuneration package of directors, is relatively modest. According to ISS, shareholder approval rates for the remuneration guidelines were 89.1% in 2010 and 99.3% in 2011. For share incentive schemes, the approval rates were 98.4% in 2010 and 99.8% in 2011. By comparison, the average approval rates in other European countries are generally lower.[273]

The one exceptional case arose in 2010 when the Swedish government voted its 37% block of shares in TeliaSonera against the company's remuneration guidelines because they contained a variable pay element.[274] As a result of the Swedish government's actions, the voting guidelines of TeliaSonera were rejected by 52% of its shareholders and the TeliaSonera board of directors had to renegotiate all of its executive employment contracts.[275]

While Swedish companies give detailed disclosures of their directors' remuneration in the minutes of the general meeting of shareholders, they provide little information about shareholder turnout and the voting results at the meeting. The minutes of the meeting seldom contain the number of shareholders that were present and the number of votes cast at the meeting. Companies only disclose that the agenda items were approved with the required majority, which is generally 50%. An exception to this rule is Lundin Petroleum, which discloses in the appendices of its report the voting record of all shareholders. In its case, the remuneration of the board of directors as well as the remuneration guidelines were approved by a large majority of the shareholders, although a number of foreign pension funds and some asset managers voted against them.[276]

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273. INSTITUTIONAL S'HOLDER SERVS., 2010 VOTING RESULTS REPORT EUROPE 22–23 (Sept. 16, 2010): INSTITUTIONAL S'HOLDER SERVS., 2010 VOTING RESULTS REPORT EUROPE15–16 (2011). The exception is 2010 when the European average was 93.3%. In that year, the lower average outcome for Sweden was due to the disapproval of the remuneration guidelines of TeliaSonera.

274. The Swedish government had banned the use of variable executive pay in wholly owned and partially owned Swedish companies in 2009.

275. For a more detailed analysis of this case, see Lekvall, *supra* note 262, at 47–49 n.4.

276. *Minutes Recorded at the Annual General Meeting of Shareholders* (Lundin Petroleum, Stockholm, Swed.), May 10, 2012, http://www.lundin-petroleum.com/Documents/ot_AGMminutes 2012_eng.pdf.

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H. The Netherlands

1. Regulatory Framework of the Dutch Board Structure and Remuneration Arrangements

Since January 1, 2013, Dutch public limited liability companies are free to choose between a one-tier and a two-tier board.[277] Before the enactment of this law, large Dutch companies had to provide a two-tier board structure with a management board and a supervisory board. While there is already a trend visible towards the one-tier board structure,[278] the large majority of the Dutch stock exchange listed companies still have two-tier boards. Consequently, we briefly address the remuneration arrangements of companies with a two-tier structure first and then discuss the differences for the one-tier board structure.

a. The Two-Tier Board Structure

Dutch listed corporations typically have a two-tier board structure.[279] The management board is responsible for the day-to-day business and affairs of the company.[280] The supervisory board's role is to supervise and advise the management board as well as to monitor the general course of the company's affairs.[281] In addition, the supervisory board chairs the general meeting of shareholders and is charged with hiring and firing the members of the management board.[282]

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277. Wet van 6 juni 2011 tot wijziging van boek 2 van het Burgerlijk Wetboek in verband met de aanpassing van regels over bestuur en toezicht in naamloze en besloten vennootschappen [Law of June 6, 2011 Changing Book 2 Civil Code Related to the Amendments of the Rules on Governance and Supervision of Public and Private Limited Liability Companies], Staatsblad van het Koninkrijk der Nederlanden [Stb.] [Official Gazette of the Netherlands], no. 275 YES, 2011, p. 1.

278. According to Eumedion, nine Dutch listed companies had opted for the one-tier board structure at the end of June 2013. *Nieuwsbrief*, EUMEDION, July 2013, at 6, *available at* http://www.eumedion.nl/nl/public/kennisbank/nieuwsbrieven/2013/nieuwsbrief_2013-06.pdf. Companies with dual listings or internationally operating companies, like Unilever or Kardan, opted for the one-tier board structure, as well as Douwe Egberts after the division from Sarah Lee, the American parent company.

279. This two-tier structure was mandatory only for a number of (large) companies, as the old regime provided exemptions for companies with mainly international activities. Many companies opt(ed) voluntarily for the two-tier structure. An analysis of the different types of two-tier structures goes beyond the purpose of this contribution.

280. Burgerlijk Wetboek [BW] [Civil code], bk. 2: 129, ¶ 1.

281. *Id.* at bk. 2: 140.

282. In fact, in a two-tier board, the appointment of a management director takes three steps. The general meeting is informed of the proposed appointment. The employee's council is requested to provide an opinion and the supervisory board appoints the director.

The general meeting of shareholders appoints the members of the supervisory board. The supervisory board must disclose its composition, size and the required expertise of its members.[283] Furthermore, the employees' council[284] has the binding right to nominate one-third of the members of the supervisory board. Supervisory board members are elected for a term of four years.

b. The One-Tier Board Structure

If a company selects a one-tier board, that board must be composed of both nonexecutive and executive members. Whether a particular candidate will be elected as a nonexecutive or executive board member is decided by the general meeting of shareholders.[285]

The Dutch Civil Code provides that the nonexecutive members of the board must monitor the performance of the executive members. Further, the chairman must be a nonexecutive member of the board of directors. In matters related to the executive compensation, all of the executive members of the board are prohibited from being involved in the decision making process as well as in the setting of their remuneration.[286]

2. Executive Remuneration

Article 135 and article 145 of Book 2 of the Dutch Civil Code detail which decision makers determine the amounts of executive remuneration and the company's remuneration policies.[287] Article 135 requires companies to develop a remuneration policy for the management board. The law does not indicate which corporate body must develop this remuneration policy. In the Dutch corporate governance code, it is considered a best practice that the supervisory board drafts the remuneration policy.[288] Companies are allowed to depart from this

283. BW bk. 2: 158, ¶ 3.

284. Companies that employ at least fifty employees must establish an employees' council. This council is composed of employees' representatives. The number of representatives lies between three and twenty-five, depending on the total number of employees. Article 6 of the Wet op de Ondernemingsraden van 28 januari 1971 [Law of 28 January 1971 on the Employees Council], Stb. 1971, p. 1.

285. BW, bk. 2: 132.

286. *Id.* at bk. 2: 129a.

287. Since 2004, Dutch listed companies must include in their annual report a description of the application of the Dutch Corporate Governance Code provisions. *Id.* at bk. 2: 391, ¶ 3.

288. It remains unclear who should draft the remuneration policy in case the company is organized with a one-tier board. The Corporate Governance Commission clarified that "the provisions that apply to supervisory directors should be immediately applied to non-executive directors in one-tier

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practice, but if they do so, they must explain the reasons therefore.[289] The proposed remuneration policy is also sent to the employees' council. The employees' council may provide the general meeting of shareholders with its opinion on the policy at the general meeting of shareholders.[290] The policy is then voted on at the general meeting of shareholders, which must approve it in order for it to become effective.[291]

If the remuneration policy for management board directors is to be amended, it must be re-approved by the general meeting of shareholders. Unfortunately, the law is silent on what constitutes an "amendment," which has led to debates about what changes are significant enough to require shareholder approval.[292] The law is also silent about whether the general meeting of shareholders has the power to amend the proposed remuneration policy itself.

The general meeting of shareholders must approve the individual remuneration packages of each management board member unless the articles of association delegate this power to another decision maker. Commonly, the articles of association delegate this power to the supervisory board so that it is unusual for individual remuneration packages to be voted on by the general meeting of shareholders.

However, the general meeting of shareholders often votes on parts of the individual pay packages for management board members. For example, if the individual director's compensation package contains any share-based remuneration, this item of the individual remuneration proposal must be submitted for shareholder approval.[293] In addition, the

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boards, with no prejudice to the other responsibilities of these non-executives." CORPORATE GOVERNANCE CODE MONITORING COMM., FOURTH REPORT ON COMPLIANCE WITH THE DUTCH CORPORATE GOVERNANCE CODE 14 (2012), *available at* http://commissiecorporategovernance.nl/monitoring-reports. It leaves the question whether the provisions that apply to the supervisory board, like developing the remuneration policy, should be applied by the nonexecutive directors jointly acting or by the board of directors including the executive directors.

289. CORPORATE GOVERNANCE CODE MONITORING COMM., DUTCH CORPORATE GOVERNANCE CODE: PRINCIPLES OF GOOD CORPORATE GOVERNANCE AND BEST PRACTICE PROVISIONS II.2.12 (2008), *available at* www.commissiecorporategovernance.nl, *archived at* http://perma.cc/4U29-RH9K.

290. BW, bk. 2: 135, ¶ 2.

291. The Dutch corporate governance code prescribes as a best practice that the supervisory board provide a "scenario analyses carried out and with due regard for the pay differentials within the enterprise" when it determines "the level and structure of the remuneration of the management board members" and must "analyse the possible outcomes of the variable remuneration components and how they may affect the remuneration of the management board members" before drafting the remuneration policy. CORPORATE GOVERNANCE CODE MONITORING COMM., *supra* note 289, at II.2.1, II.2.2.

292. *See* EUMEDION, EVALUATIE AVA-SEIZOEN 9–10 (2012), *available at* http://www.eumedion.nl/nl/public/kennisbank/ava-evaluaties/2012_ava-evaluatie.pdf (last visited July 10, 2013).

293. BW, bk. 2: 135, ¶ 4.

proposal must provide information on the maximum number of shares or options that can be granted to the board as well as the criteria for granting. Notwithstanding the shareholder meeting's approval right, the corporate body that contracts with the candidate-director can validly represent the company even if the approval is missing or the granting is disapproved.

Furthermore, the Dutch Parliament recently approved the law to provide for claw-back provisions for bonus awards that have been granted based on incorrect information. Under the terms of this law, a representative elected by the general meeting of shareholders, or another body specified in the articles of association, will have the right to modify the bonus if it is determined to be unreasonable and unfair.[294] This provision was already incorporated in the corporate governance code as a best practice.[295]

Finally, article 145 of Book 2 of the Dutch Civil Code provides that the general meeting of shareholders can fix the compensation of the members of the supervisory board. It is common practice that the supervisory board proposes a fixed, flat cash compensation payment for each member of the board, which is then submitted to the company's general meeting of shareholders for approval.

3. Assessment of Say on Pay

Since 2005, the general meeting of shareholders must approve the company's remuneration policy and any amendments to this policy.[296] Using this vote, shareholders can exert substantial influence on a listed company's remuneration policy. The intensity of shareholder consideration of remuneration policies is revealed in the minutes of the meeting of many companies. These minutes show that corporate remuneration policies, as well as individual management director remuneration packages, are regularly and heavily debated, although actual rejections of either of them are rare. A more recent phenomenon is the voting against the discharging of the supervisory board members when the

294. Wet van 11 december 2013 tot wijziging van boek 2 van het Burgerlijk Wetboek en de Wet op het financieel toezicht in verband met de bevoegdheid tot aanpassing en terugvordering van bonussen en winstdelingen van bestuurders en dagelijks beleidsbepalers [Law of December 2013 Changing Book 2 Civil Code and the Law of Financial Supervision Related to the Power to Modify and Claw Back of Bonuses of Directors and Executive Officers], Stb. 2013, no. 563YES, p. 1.

295. CORPORATE GOVERNANCE CODE MONITORING COMM., *supra* note 289, at II.2.10.

296. The version of article 135 that requires the general meeting of shareholders to approve the remuneration policy was enacted in Wet van 9 juli 2004 tot wijziging van boek 2 van het Burgerlijk Wetboek in verband met aanpassing van de structuurregeling [Law of 9 July 2004 to Amend Book 2 of the Civil Code Related to the Structure Regime], Stb. 2004, p. 1.

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discretionary power of this board to change—i.e., lower—the performance criteria of the remuneration package of the management board members.[297]

Every year, Eumedion[298] reports on the developments at general meetings of shareholders. The remuneration policy is one of the governance items that Eumedion regularly addresses in its reports to its institutional investor clients. Since 2008, Eumedion has identified several trends in the participation of shareholders in the remuneration debate.[299]

First, shareholders generally do not strongly oppose companies over their remuneration policies. Table 2 below shows the eleven remuneration votes that generated the highest levels of shareholder opposition at general meetings of AEX companies between 2008 and 2012.[300] Generally, it appears that shareholders consider company-specific arguments when voting. In particular, when the performance criteria for variable pay are insufficiently detailed or perceived by shareholders to be too generous, many shareholders will vote against the remuneration policy, or the remuneration item.

Since 2011, Eumedion also reports the recommendations of the third party voting advisor ISS, and additionally in 2012 those of a second proxy voting advisor, Glass Lewis. As Table 2 shows, there were three remuneration issues where ISS issued a negative recommendation on the proposal. However, Eumedion reports that, in 2012, in thirty-one out of forty-six highly contested agenda items (67%) both ISS and Glass Lewis supported the companies' proposals, while an additional nine (19.5%) more were only opposed by one of these proxy advisors. Based on these results, Eumedion argues that the impact of the proxy advisors' voting recommendation does not appear to determine the outcome of the shareholder vote.[301]

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297. A large majority of the minority shareholders disapproved this change by the supervisory board of Heineken. Other cases are reported by Eumedion, EUMEDION, EVALUATIE AVA-SEIZOEN 14 (2014), *available at* http://www.eumedion.nl/nl/public/kennisbank/ava-evaluaties/2014-ava-evaluatie.pdf (last visited Aug. 20, 2014).

298. Eumedion represents approximately seventy institutional investors, managing more than €1 trillion in assets, and its major goals are to enhance corporate governance, environmental and social performance and strategy. For more information, see *Corporate Governance Forum*, EUMEDION, www.eumedion.nl.

299. EUMEDION, *supra* note 292.

300. These are taken from Eumedion's yearly top ten lists of opposed items.

301. EUMEDION, *supra* note 292, at 13.

TABLE 2: REMUNERATION ITEMS AMONGST TOP 10 OPPOSITION ITEMS AT AEX AGMS 2008–2012

Company	Year	Voting item	Against	W/hold	Result	ISS rec.
Philips	2008	Change LTIP	57.8	5.2	Rejected	
Shell	2008	Granting retention bonus	23.5	25.9	Accepted	
SBM Offshore	2008	Changing remuneration policy	41.1	4.5	Accepted	
Shell	2009	Remuneration report	57.1	3.9	Rejected	
ASML	2009	Right to issue 'sign on' shares	41.1	0.3	Accepted	
ASML	2009	Right to issue 'sign on' options	0.8	28.7	Accepted	
Heineken	2010	Changing remuneration policy	17.6	0.4	Accepted	
Heineken	2010	Changing LTIP	16.6	0.4	Accepted	
ING	2011	Changing remuneration policy	43.2		Accepted	Against
Aegon	2011	Changing remuneration policy	30.3		Accepted	Against
TNT Express	2012	Remuneration superv. board	30.1		Accepted	Against

Source: Eumedion, *Evaluatie AVA Seizoen*, 2008, 2009, 2010, 2011, 2012. (www.eumedion.nl).

Table 2 emphasizes the remuneration items that experienced significant opposition. However, the general level of voting disapproval of the remuneration policy is much lower. We studied all remuneration related issues at the general meetings of AEX companies in 2010, 2011 and 2012. These results are in Table 3.

TABLE 3: APPROVAL OF REMUNERATION ITEMS AT AGMS OF AEX COMPANIES IN 2010, 2011 AND 2012

	2010	2011	2012	All
Avg. approval rate	96.58	86.42	87.97	91.46
Remuneration policy	95.58	83.00	88.97	89.52
Other pay issues	97.25	89.41	86.71	92.88
Total number items	20	15	9	44

Source: Authors' research based on the minutes of the general meetings of AEX companies

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The 2010 results are distorted by the 2008 changes to the Dutch corporate governance code that led many companies' boards to reconsider their remuneration policy in 2009, which then had to be approved at the 2010 AGM. As the amended policies were changed only to reflect new best practice amendments, shareholder approval rates were unusually high.

The amendments to remuneration policies in 2011 and 2012 are more representative as they involved company-specific factors. For these years, we see higher levels of shareholder opposition, although the mean opposing rate is still significantly lower than the disapproval levels that were reported in Table 2. In results not tabulated, we find that there are no statistically significant differences between the approval rates of corporate remuneration policies versus those for all other remuneration items, like the approval of long term investment plans, bonus shares, etc.

What these tables do not show are several remuneration agenda items that have been withdrawn before a shareholder vote. Eumedion provides evidence that many (institutional) shareholders perform a detailed study of the agenda of the meeting, including the proposal to change the remuneration policy, or other remuneration related proposals, and then contact the company before the general meeting takes place to express their displeasure. In cases in which the management board of directors and supervisory board believe that the shareholder opposition against the item is very significant, the board may withdraw the item from the shareholder meeting's agenda. Eumedion believes that this practice creates a healthy dialogue between the remuneration committee and the shareholders that helps to identify the sensitivity of remuneration items earlier so that the company can avoid having to withdraw highly opposed agenda items.[302]

Dutch law contains some ambiguities on the appropriate Say on Pay framework that require some further legislative consideration. First, as we discussed above, material changes to a company's remuneration policy must be approved by the shareholders. There remains significant debate as to the meaning of "material". For example, one company asked its AGM to approve a change of its peer group that it used in determining the short- and long-term management bonuses, while another company decided that the supervisory board could make changes to the composition of the peer group without asking the company's shareholders.[303] Second, many shareholders complain that companies need to disclose more information, particularly about performance-based remuneration packages and the

302. EUMEDION, EVALUATIE AVA-SEIZOEN 10 (2008).
303. *Id.* at 5.

http://openscholarship.wustl.edu/law_lawreview/vol92/iss3/7

discretionary power of the supervisory board over how it will execute an approved policy.

Finally, remuneration policies need regular modifications to reflect changes in circumstances. For example, while during the beginning of the 2000s many companies used total shareholder return as the most important performance measure for bonuses, recently they have moved to more general performance-based measures like corporate social responsibility, sustainable development, etc.[304] This change in metrics will necessitate a new remuneration policy vote.

New regulatory or legislative initiatives may also create a need to modify remuneration policies. This would be the case for banks, as they needed to amend their remuneration policies to align the short- and long-term bonus schemes with the transposed provision of the Capital Requirements Directive III.[305] Another example would be that many companies introduced claw-back provisions for bonuses into their policies to comply with best practices as set forth in the Dutch corporate governance code,[306] which recently became law.

I. Summary of Countries' Different Features

Table 4 below summarizes the board structures and overall shareholder voting rules for the eight countries discussed above. We can see several important differences. First, board structure matters: in countries with two-tier boards, historically the supervisory board usurped a number of powers generally assigned to the shareholders in a one-tier board structure. Most importantly for our purposes, is that one of the assigned powers to the supervisory board was the setting of the remuneration of management board members. Recent developments in the two-tier regime countries seem to reassign the power to set the remuneration (policy) back to the shareholders.

Second, the contours of "Say on Pay" vary significantly across countries. The gamut of regimes runs from setting the individual pay package of (executive) directors in the U.S. to advising the remuneration policy in Sweden to voting on the remuneration report in the U.K. and Belgium. In this setting, shareholders of Swedish companies set the future in corporate pay packages, while the British shareholders must be satisfied with the approval of "past" remuneration schemes.

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304. EUMEDION, EVALUATIE AVA-SEIZOEN 10 (2011).
305. This has been overruled by the 2013 CRD IV Directive.
306. EUMEDION, EVALUATIE AVA-SEIZOEN 5–6 (2010).

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Third, in most countries, shareholder votes on executive remuneration matters advise the board of directors in its development of appropriate incentivizing schemes of executive directors, while other countries empower the general meeting of shareholders to bindingly set the remuneration (policy). Fourth, "Say on Pay" sometimes means "Say on Individual Pay" while in other countries it means "Say on Group Pay." For example, most German companies provide shareholders with an advisory vote of the remuneration system of the management board, but it belongs to the powers of the supervisory board to set the individual remuneration package of a management board member. In comparison, at Swedish companies the remuneration package of directors is determined individually. Finally, "Say on Pay" is not always an annual experience: under American law, it can take up to three years before a shareholder can have her say, whereas in the Netherlands, it can even take longer if the previously approved policy remains unchanged.

The many differences between the different "Say on Pay" regimes complicate the choices facing policy makers in the individual countries. The development of a European "Say on Pay" regime illustrates the difficulties. For nonfinancial companies, 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.[307] 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.[308] 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).

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307. *Commission Green Paper, The EU Corporate Governance Framework*, at 23, COM (2011) 164 final (Apr. 5, 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 December 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 April 2009 on Remuneration Policies in the Financial Services Sector, O.J. (L 120) 22–27 (EC).

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

In its December 2012 Communication,[309] the European Commission revealed that it would make a shareholder vote on both the remuneration report and the remuneration policy mandatory,[310] probably through a modification of the Shareholder Rights Directive.[311] 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.[312] 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.[313] In April 2014 this proposal for a European Directive was issued.[314] The European Commission proposes to have the remuneration policy of public listed entities "as regards directors" approved by the shareholders at least every three years. 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.[315] This proposal will be heavily debated in the upcoming period and it is far from sure the amendments to the Shareholder Rights Directive will be approved.

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

310. *Id.* at 9.

311. 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).

312. *Communication of the Commission*, *supra* note 309, at 8.

313. *Id*. at 10.

314. *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 (May 9, 2014), *available at* eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2014:2013:FIN.

315. *Id.* art. 9a, art. 9b.

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Table 4: What Do Shareholders Vote On?	Belgium	France	Germany	The Netherlands	Sweden	UK	US	Australia
Board type	One tier	One or two tier	Two tier	One or two tier	One tier	One tier	One tier	One tier
Vote to determine compensation of board membership	Binding	Binding	N/A	Yes but can be delegated (expected to be	Binding	N/A	N/A	N/A
Vote on compensation of management directors for their executive duties (only for one tiered	N/A	Advisory (after 2014)	N/A	Yes but can be delegated (expected to be common)	Binding	N/A	Mandatory, AdvisoryN/A	N/A
Frequency of Vote	Yearly	Yearly	Not defined	When policy is changed	Yearly	Yearly	At least every three years	Yearly
Vote to approve remuneration policy of the board	N/A	N/A	N/A	Yes	Yes	N/A	N/A	N/A
Vote to approve remuneration report	Mandatory advisory	N/A	N/A	N/A	N/A	Mandatory advisory	N/A	Mandatory, advisory
Vote to approve the remuneration package of executive board members (two tiered board)	N/A	Advisory	N/A	Yes but can be delegated (common)	N/A	N/A	N/A	N/A
Vote to approve of the remuneration system of the management board (only for two tiered boards)	N/A	N/A	Yes, advisory	N/A	N/A	N/A	N/A	N/A
Vote to determine compensation of supervisory board (only for two tiered boards)	N/A	Yes, mandatory	Yes, mandatory	Yes, mandatory	N/A	N/A	N/A	N/A

II. WHY IS SAY ON PAY BEING ADOPTED?

A. Diverse Versus Concentrated Ownership Patterns

One factor that may influence the adoption of Say on Pay in a country is whether the predominant form of ownership structure is diverse or concentrated. The U.S., the U.K., and to a lesser extent Australia, are good examples of dispersed-ownership systems. At publicly traded corporations with highly dispersed share ownership, managerial agency costs are an important problem, but shareholder monitoring has historically been weak because of collective action problems. [316] These managerial agency costs may be reduced if we can align managers' and shareholders' interests through the use of stock options and long term incentive pay. U.S. and U.K. firms rely on incentive pay systems to more closely align the interests of managers and shareholders.[317] Australian executives also receive substantial amounts of restricted stock and stock options.[318]

From the perspective of corporate executives, however, substituting stock options or restricted stock for other forms of fixed compensation increases the riskiness of their pay package, especially when stringent corporate performance conditions are attached to these awards. In response to the greater risk, managers discount substantially the value of performance-based pay awards.[319] To keep pay levels at a specified amount, companies must, for example, offer more stock options to compensate for the higher risks of little or no return if the options fail to pay off.

Reflecting their views on the tradeoff between improved alignment of incentives and higher costs, institutional shareholders in American and U.K. firms have generally been content to see executive pay rise substantially so long as the increase has been incentive-oriented.[320] In the post-financial crisis era, however, institutional investors have become

316. Cheffins & Thomas, *supra* note 3, at 308, 312.

317. Brian R. Cheffins, *Current Trends in Corporate Governance: Going from London to Milan via Toronto*, 10 DUKE J. COMP. & INT'L L. 5, 14–15, 17 (1999).

318. Randall S. Thomas, *Lessons from the Rapid Evolution of Executive Remuneration Practices in Australia: Hard Law, Soft Law, Boards and Consultants*, *in* RESEARCH HANDBOOK ON EXECUTIVE PAY, *supra* note 2, at 341, 350–51.

319. *See, e.g.*, Brian Hall & Kevin J. Murphy, *Stock Options for Undiversified Executives*, 33 J. ACCT. & ECON. 3, 4–5 (2002); Lisa K. Meulbroek, *The Efficiency of Equity-Linked Compensation: Understanding the Full Cost of Awarding Executive Stock Options*, FIN. MGMT., Summer 2001, at 5.

320. Cheffins & Thomas, *supra* note 3, at 294, 312 (noting that British shareholders might be more prepared to take a stand against high pay arrangements than American investors).

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more critical of high executive pay levels at firms that are performing poorly.[321]

Say on Pay voting systems in diffuse ownership countries give investors a mechanism for drawing attention to their concerns about excess, or poorly structured, incentive pay. If corporate boards make pay awards that are out of line with corporate performance, or with those given to executives at comparable firms in similar industries, the firm risks a "failed" Say on Pay vote and the resulting negative attention that is focused on its directors in the aftermath of such a vote. In extreme cases, a board's failure to respond appropriately to a weak Say on Pay vote may also attract the attention of an activist hedge fund, as may have occurred recently at Hess Oil.[322]

In Continental Europe, where concentrated share ownership was, or is, the norm, Say on Pay may be less important as a means of mobilizing shareholder opposition against high executive pay levels. In these countries, control is concentrated in the hands of a shareholder group, which therefore can discipline ineffective managers,[323] so that incentive pay systems are less important and executive pay levels are correspondingly lower.[324] Overall pay for performance levels will be lower, and the use of stock options less common, than in dispersed-ownership countries. Studies by Brunello,[325] Ramaswamy, Veliyath, and Gomes,[326] and Park, Nelson, and Torabzadeh,[327] provide empirical evidence from Canada, India, and Italy, which supports these claims.

If ownership concentration levels should decline, however, it is likely that executive pay levels and performance-based compensation will increase in the future as a means of aligning managers' incentives with those of the shareholders. This stronger alignment may offset the loss of monitoring when the control shareholder disappears. This is particularly likely if the cause of increased dispersion is growing levels of foreign

321. Thomas et al., *supra* note 6.

322. Daniel Gilbert & Joann S. Lublin, *Board Pay Fuels Hess Battle*, WALL ST. J., Mar. 26, 2013, at B8.

323. Brian R. Cheffins, *Minority Shareholders and Corporate Governance*, COMPANY LAW., Feb. 2000, at 41.

324. Todd T. Milbourn, *Financial Systems and Corporate Governance* 154 J. INST'L & THEORETIC'L ECON. 170, 174 (1998).

325. Giorgio Brunello et al., *Executive Compensation and Firm Performance in Italy*, 19 INT'L J. INDUS. ORG. 133, 141, 155 (2001).

326. Kannan Ramaswamy et al., *A Study of the Determinants of CEO Compensation in India*, 40 MGMT. INT'L REV. 167, 182–83 (2000).

327. Yun W. Park et al., *Controlling Shareholder and Executive Incentive Structure: Canadian Evidence*, 17 CAN. J. ADMIN. SCI. 245, 246 (2000).

portfolio investment by U.S. and U.K. institutional investors.[328] Consistent with this thesis, Thomas finds some evidence that over time, shareholder ownership in Sweden and Germany has become less concentrated and executive incentive compensation (and overall pay levels) is rising.[329]

For instance, traditionally corporate control in Sweden has been heavily concentrated in the hands of one or two family shareholders[330]: as of 1998, in listed Swedish companies, on average, the largest shareholder controlled 38% of the voting rights, which in practice implied operational control of the company.[331] However, in recent years, share ownership in Sweden has become more dispersed in part because of a new Swedish pension model that has created large state-controlled and corporatist pension funds that have invested heavily in Swedish firms.[332] Foreign investment also has increased dramatically—in the early 1990s, foreign investors owned less than 10% of Swedish listed companies' stock, whereas by 2012 foreign ownership of Swedish shares rose to 40.3% of all shares.[333] Amongst the foreign investors, American institutions were the largest single group, holding roughly 29% of the total equity of Swedish companies. As a result, commentators predict that Swedish firms' formerly concentrated family ownership model will likely give way to more dispersed ownership by foreign owners and state or corporate pension funds.[334]

Executive pay is likely to be affected by these changes. Previously, concentrated ownership reduced the level of CEO compensation in Swedish and Norwegian firms because large owners are better at

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328. William W. Bratton & Joseph A. McCahery, *Comparative Corporate Governance and the Theory of the Firm: The Case Against Global Cross Reference*, 38 COLUM. J. TRANSNAT'L. L. 213, 234 (1999); Mary O'Sullivan, *Corporate Governance and Globalization*, 570 ANNALS AM. ACAD. POL. & SOC. SCI. 153, 167 (2000).

329. Randall S. Thomas, *International Executive Pay: Current Practices and Future Trends*, *in* LABOR AND EMPLOYMENT LAW AND ECONOMICS 197–98 (Kenneth G. Dau-Schmidt, Seth D. Harris & Orly Lobel eds., 2009).

330. Magnus Henrekson & Ulf Jakobsson, *The Swedish Model of Corporate Ownership and Control in Transition in* WHO WILL OWN EUROPE? THE INTERNATIONALISATION OF ASSET OWNERSHIP IN EUROPE (Harry Huizinga & Lars Jonung eds., Cambridge: Cambridge University Press 2005), *available at* http://ssrn.com/abstract=998256.

331. *Id.* at 27. In 34% of the firms, the controlling owner had more than 50% of the votes, while in 82% of the firms, there was a well-defined owner holding more than 25% of the votes. *Id.*

332. *Id.* at 1.

333. Officiella Statistik, *Aktiägande i Bolag Noterade pa Svensk Marknadsplats*, STATISTIKA MEDELLANDEN (Dec. 2012), *available* at http://www.scb.se/Statistik/FM/FM0201/2012H02/FM0201_2012H02_SM_FM20SM1301.pdf.

334. Henrekson & Jakobsson, *supra* note 330, at 34.

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monitoring CEOs directly.[335] Today, however, we are moving towards a more dispersed ownership in public corporations which could lead to increased remuneration because of decreased control shareholder monitoring of pay levels. This suggests a potential need for new monitoring mechanisms for shareholders in Sweden. Perhaps this is why, as ownership concentration levels dropped, and executive pay levels escalated, Sweden enacted binding Say on Pay legislation.

Many German public companies have experienced similar shifts in their shareholder composition over the last decade. In the past, the largest German companies were controlled by domestic investors, banks, insurance companies and families.[336] In addition, the state controlled important German companies, such as the Deutsche Post and Deutsche Telekom.[337] Today things have changed: 53% of the shares on the DAX, the stock index for the thirty largest German companies, are in foreign hands.[338] Moreover, there has been a significant decrease in ownership concentration levels since 2000: the largest shareholder's average voting block at a DAX-30 company decreased from 26.4% in 1999 to 20.4% in 2012.[339] This resembles the ownership concentration levels found in the UK.[340] Finally, only four companies are still majority controlled, while one-half of the DAX companies have no shareholders owning more than 10% of the voting rights.[341]

Concentrated ownership by banks, all other things being equal, is associated with lower levels of CEO compensation at German companies.[342] Pay-for-performance sensitivities are very low and

335. Lars Oxelheim & Trond Randøy, *The Anglo-American Financial Influence on CEO Compensation in Non-Anglo-American Firms*, 36 J. INT'L BUS. STUD. 470 (2005).

336. WOLFGANG STREECK & MARTIN HÖPNER, ALLE MACHT DEM MARKT? FALLSTUDIEN ZUR ABWICKLUNG DER DEUTSCHLAND AG 120 (Martin Höpner ed., 2003).

337. *Id.* at 120.

338. Thomas, *supra* note 329, at 198. The DAX measures the performance of the Prime Standard's thirty largest German companies in terms of order book volume and market capitalization. DEUTSCHE BÖRSE GROUP, http://deutsche-boerse.com/dbag/dispatch/en/isg/gdb_navigation/home?active=overview&timespan=1d&wpbpl=&wp=DE0008469008&foldertype=_Index&wplist=DE0008469008&module=InOverview_Index.

339. Christoph Van der Elst, *The Influence of Shareholder Rights on Shareholder Behavior*, 5 CORP. FIN. & CAP. MKTS. L. REV. 50, 56 (2010); authors' own research based on companies' annual reports and websites (May 2013) (on file with authors).

340. In 2007, the average voting block of a sample of UK companies was 19% of the votes. C. Van der Elst, *Shareholder Mobility in Five European Countries*, *in* CORPORATE MANAGEMENT: SHAREHOLDER RIGHTS 211 (L. Padmavathi ed., 2009).

341. Authors' own research based on companies annual reports and websites (May 2013) (on file with authors).

342. Alfred Haid & B. Burcin Yurtoglu, *Ownership Structure and Executive Compensation in Germany* 15, 19 (Working Paper 2006), *available at* http://ssrn.com/abstract=948926. Interestingly,

concentrated ownership reduces them still further.[343] Conversely, as ownership concentration disperses, we should expect to see higher levels of executive compensation. As an example, the mean compensation of a member of the management board of a DAX company soared from €1.2 million in 2001 to over €3.0 million in 2013, an increase of over 250%, whereas the average annual wage for workers increased only 18% during the same period.[344]

As ownership concentration levels have dropped in Germany, the country has also moved to give shareholders more "say" about executive pay. The Law on the Appropriateness of Director Compensation states that the general meeting of shareholders can be provided an advisory vote of the remuneration system of the management board of listed companies.[345] Further, institutional investors make use of advisory Say on Pay votes to signal their worries over pay increases.[346]

Recently, in the aftermath of several pay scandals, as well as Switzerland's popular referendum in support of a binding Say on Pay vote for Swiss firms, there has been strong pressure on the government to introduce a binding Say on Pay vote in Germany. The German government wants to move "Say on pay for listed companies to a mandatory system [that will be] . . . binding for the supervisory board."[347] For some members of the German Parliament, these new proposals are insufficient: they want to limit directly executive pay to a maximum of a fixed multiple of the ratio of the total pay of a member of the management board to the average remuneration of the employees of the company. This cap would be binding, and would have to be determined by the supervisory board and disclosed in the company's annual report to its shareholders.[348]

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family ownership of German firms increases compensation, *id.*, perhaps because families use it as a mechanism for diverting value to themselves.

343. *Id.*

344. *OECD.StatExtracts*, ORG. FOR ECON. CO-OPERATION & DEV. (2013), http://stats.oecd.org/# (last visited May 28, 2013).

345. AktG, at § 120, para. 4. The law only requires that the company allows the general meeting to vote on the remuneration system of the management board; there is no mandatory requirement.

346. Madison Marriage, *Hermes Attacks Deutsche Pay Levels*, FIN. TIMES, May 27, 2013, at 1.

347. Free translation of: "'Say on pay' soll für börsennotierte Aktiengesellschaften zu einem obligatorischen und für den Aufsichtsrat verbindlichen Element ausgebaut werden," Press Release, Die Bundesregierung, Vernunft und Maß bei Managerbezahlung (May 8, 2013) (http://www.bundesregierung.de/Content/DE/Artikel/2013/05/2013-05-08-kabinett-aktiengesetz.html), *archived at* http://perma.cc/SU9R-QLAJ.

348. Press Release, Deutscher Bundestag, SPD will Managereinkünfte Beschränken, DEUTSCHER BUNDESTAG (May 16, 2013) (http://www.bundestag.de/presse/hib/2013_05/2013_273/04.html), *archived at* http://perma.cc/7YXW-28PP.

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France experienced a similar ownership development. In 1999, the companies in the CAC-40 index had a major shareholder with an average voting block of 28.1%. Gradually, the ownership structure of the largest companies became more dispersed. In 2005, the voting block of the largest shareholder dropped to 25.6%, then in 2007, decreased further to 22.2%, and most recently was at 21.1% by the end of 2012.[349] At the same time as control blocks were shrinking, the French government, first in 2005, and later in 2007, gave the general meeting of shareholders the right to vote on the termination payments to be made to an executive board member, as well as a vote on whether to permit a corporate board to grant stock options. The French also introduced a maximum remuneration cap for government-controlled companies. Finally, France introduced a more general comply-or-explain vote on the entire compensation package of top executives.[350]

While it would be a mistake to draw too-broad conclusions from the experience of these three countries, it does appear that shifts in ownership concentration levels, particularly at large listed companies, are an important factor behind at least some countries' adoption of the Say on Pay vote. However, even in countries where control shareholders continue to reign supreme, Say on Pay may provide control shareholders with an additional mechanism to control executive pay, and allow family-run companies to claim that they are taking action against negative social reactions to "too high" levels of executive pay. "No" votes on Say on Pay proposals may also provide minority shareholders with a mechanism for expressing their opposition to executive pay practices.

B. The Effects on Executive Compensation of Increased Stock Ownership by Institutional Investors

A second important factor to consider is the institutionalization of stock ownership. Particularly in the U.S. and U.K., institutional share ownership has greatly evolved in the past several decades, and as the size of institutional investors has grown, they have expanded their portfolios to include large quantities of foreign equity securities. In addition, the abolishment of national stock ownership restrictions, and the globalization of international markets, has provided investors with many new

349. Van der Elst, *supra* note 339, at 56; Authors' own research based on companies annual reports and websites of these companies (May 2013) (on file with authors).

350. See *supra* Part I.E for further discussion.

investment opportunities and a large shift towards international stock.[351] As a result, in most countries, the shareholder base of large public companies has internationalized.

Table 5 illustrates this shift. In most of the countries covered by the table, the share of stock in hands of foreign shareholders more than doubled between 1995 and 2010, although the financial crisis of 2008 partly reversed this trend. In 2010, foreign investors' ownership share ranged from a low of 13% of the shares of American companies to a high of 65% of the shares of Dutch companies. This represents a marked increase from the number in 1995 (U.S. 6%; Dutch 37%). More generally, in countries like France, Sweden, Belgium and the UK, foreign shareholders control close to 40% of the shares in more recent years.

TABLE 5: EVOLUTION OF STOCK IN THE HANDS OF FOREIGN SHAREHOLDERS

	1995	2000	2005	2007	2010
Belgium	22.9%	31.1%	36.2%	38.7%	N/A
France	24.9%	38.8%	40.5%	41.1%	38.7%
Germany	8.2%	12.5%	18.4%	21.3%	N/A
The Netherlands	37.0%	N/A	75.0%	71.0%	65.0%
Sweden	29.6%	39.0%	35.3%	38.0%	37.8%
UK	16.3%	35.7%	36.3%	40.0%	41.2%
US	5.7%	8.4%	9.9%	11.0%	13.3%

Sources for Table 5: Belgium, France, Germany: FESE, Share Ownership Structure in Europe, 2008, at 112; France 2010: AFG, Contribution des OPCVM aux fonds propres des entreprises, 2011, at 6; The Netherlands: 1995 and 2005: R. Abma, Het aandeelhoudersvergaderingenseizoen 2006: feiten en trends, Tijdschrift voor Ondernemingsbestuur, 2006 nr. 5, 169; 2007, FESE; 2010: own calculations based on Nyenrode Business Universiteit, Naleving Nederlandse Corporate Governance Code 2012, at 36; Sweden: SCB, Aktieägarstatistik, 2013 at 24; UK (data 1994, 2004, 2006 instead of 1995, 2005, 2007): ONS, Ownership of UK Quoted Shares 2010; US: Census table 1201 (data 1994, 2004, 2006 instead of 2000, 2005, 2008, 2009, 2010).

351. For a detailed analysis of the globalization of a number of capital markets, see Maurice Obstfeld & Alan M. Taylor, *Globalization and Capital Markets*, *in* GLOBALIZATION IN HISTORICAL PERSPECTIVE 122–87 (Michael D. Bordo, Alan M. Taylor & Jeffrey G. Williamson eds., 2003).

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To try to examine these effects more closely, we look at German data. Many German companies regularly investigate their shareholder base and disclose information about the importance and origins of these investors. This information is split in a regional breakdown of the ownership of the shares and the relative importance of institutional investors and private investors (and sometimes other classes). We used these companies' reports to estimate the importance of the institutional investors coming from the different regions in the world.[352] Our data is taken from December 2012 to April 2013. According to our survey of 24 DAX companies,[353] institutional investors control between 7%[354] and 93%[355] of their shares, with a mean stake of almost 68%.[356] Approximately 19% of their stock is held by German institutional investors while another 50% is in the hands of foreign institutional investors. American and UK institutional investors are the most important kind of foreign shareholders with American institutions controlling 19% and U.K. firms controlling another 11% of these German companies' shares.[357]

For a broader set of Western European countries, data collected by one of the authors shows the relative importance of certain types of institutional investors: banks, investment funds, and hedge funds/private equity funds.[358] As shown in Table 6, foreign investment funds, private equity and hedge funds became important shareholders of Belgian, French and German companies and they consolidated their positions in UK companies in the last decade.

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352. The estimation provides only a first, rough indication: it is assumed that private investors and institutional investors are proportionally spread over the different regions.

353. The other six companies did not disclose the ownership structure or only disclosed very general data.

354. VOLKSWAGEN, ANNUAL REPORT 2012, at 169 (2013).

355. Aktionärsstruktur der Gruppe Deutsche Börse, *available at* http://deutsche-boerse.com/dbg/dispatch/de/kir/dbg_nav/investor_relations/20_The_Share/40_Shareholder_Structure (last visited 28 May, 2013).

356. Majority controlled companies like Beiersdorf and Merck do not disclose detailed information of the region of the investors. This explains this high percentage.

357. Many companies do not distinguish between US and Canadian institutional investors and British and Irish institutional investors.

358. Christoph Van der Elst, *Are Shareholder Rights Appealing to Foreign Shareholders?*, *in* FESTSCHRIFT FÜR KLAUS HOPT 629–44 (Stefan Grundmann, Brigitte Haar, Hanno Merkt, Peter O. Mülbert & Marina Wellenhofer eds., 2010)).

TABLE 6: RELATIVE IMPORTANCE OF FOREIGN INVESTMENT FUNDS, FOREIGN HEDGE FUNDS, FOREIGN PRIVATE EQUITY FUNDS AND FOREIGN BANKS IN FOUR WESTERN EUROPEAN COUNTRIES

1999	Belgium	France	Germany	UK
Investment funds	N/A	2.31%	2.18%	8.96%
Hedge funds/private equity	N/A	N/A	N/A	N/A
Banks	N/A	1.73%	N/A	2.03%
2007	Belgium	France	Germany	UK
Investment funds	7.14%	14.75%	3.77%	8.71%
Hedge funds/private equity	N/A	2.19%	4.56%	0.11%
Banks	0.48%	1.64%	2.18%	4.95%

Source: C. Van der Elst, *Are Shareholder Rights Appealing to Foreign Shareholders?*, in FESTSCHRIFT FÜR KLAUS HOPT, 636 (Stefan Grundmann, Brigitte Haar, Hanno Merkt, Peter O. Mülbert & Marina Wellenhofer eds., 2010).

Many of these investors have either a legal duty to vote their shares (the institutional investors) or want to actively make use of their voice in the investee companies (particularly the activist hedge funds). Institutional investors are also likely to have retained a proxy voting advisor to give them information or voting advice about the Say on Pay vote to help solve the collective action problem. These third-party voting advisors provide valuable information about the various items that shareholders vote on as well as voting recommendations that may assist the institutional shareholders in casting their ballots. To the extent that these third-party voting advisors have promulgated corporate governance, or compensation, guidelines that shape their voting recommendations, they may have an independent additional effect on executive pay levels and composition.[359]

Foreign institutional investors actively strive for long-term performance and encourage the use of pay for performance. As noted in Part I, executive performance-based pay is considered an important remedy for agency problems and long-term incentive pay for senior managers can serve as the best proxy for the alignment of the interests of shareholders and management. With the institutions' support, many companies' executives were provided with performance-based pay, including stock options. If remuneration schemes are appropriately

359. Thomas et al., *supra* note 6.

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designed to reflect shareholder value, this could result in better shareholder returns.

However, in the period following the financial crisis, it became clear that incentive contracting can also be part of the agency problem at companies with poor corporate governance practices, as witnessed by overly generously designed packages, backdating of stock options and the sometimes modest connections between better performance for high pay. If shareholders are provided with Say on Pay, they can monitor incentive arrangements and remuneration packages by using this mechanism to tell management their views on pay issues. Hence, we would expect that increased levels of foreign institutional share ownership would lead to greater calls for implementation of Say on Pay votes.

C. Social Intolerance of Income Inequality

Cultural differences,[360] or more particularly differences in the level of social tolerance for high levels of pay disparities, may exist between different countries.[361] For example, Americans may be more tolerant of income inequality that is perceived to arise out of differences in "effort, talent or entrepreneurial risk taking,"[362] so that investors in the U.S. may accept high levels of pay for performance as part of executive pay packages.[363] By contrast, in other countries, a stronger sense of egalitarianism could suppress high CEO pay,[364] and conspicuous displays of wealth. Even dispersed-ownership countries like the U.K.[365] and Canada,[366] which supposedly have adopted the American business

360. Culture can be defined as a society's shared values, understandings, and assumptions. HELEN DERESKY, INTERNATIONAL MANAGEMENT: MANAGING ACROSS BORDERS AND CULTURES 15 (3d ed., 2000).

361. Herbert A. Henzler, *The New Era of Eurocapitalism*, HARV. BUS. REV., July–Aug. 1992, at 60.

362. Martin J. Conyon & Kevin J. Murphy, *The Prince and the Pauper? CEO Pay in the United States and the United Kingdom*, 110 ECON. J. F640, F667 (2000).

363. James Cox, *US Success Draws Envy, Protests*, USA TODAY, Aug. 3, 2000, at B1; Michael Crawford, *Peanuts for Elephants*, CAN. BUS., July 1994, at 16; Maria Slade, *NZ Executives Pay Third World Salaries*, INDEP. BUS.WKLY., Sept. 26, 1997, at 23. For anecdotal evidence consistent with this view, see David Leonhardt, *Executive Pay Drops off the Political Radar*, N.Y. TIMES, Apr. 16, 2000, at Week in Review 5.

364. Shirley Fung, *How Should We Pay Them?*, ACROSS THE BOARD, June 1999, at 36, 39; Tara Parker-Pope, *Culture Clash: Do US-Style Compensation Plans Make Sense in Other Countries?*, WALL ST. J., Apr. 12, 1995, at R7.

365. Conyon & Murphy, *supra* note 362, at F667–68; Martin Van der Weyer, *Too Much Cream?*, INDEP., Aug. 16, 1998, at 16.

366. Crawford, *supra* note 363, at 16.

culture,[367] may be influenced by this factor. Similarly, in Australia, the comparatively modest managerial pay arrangements in that country may be influenced by concerns about out-of-line pay arrangements.[368] If culture is important, it could lend strength to claims that shareholders need to have a vote on executive remuneration arrangements in order to keep pay disparities from getting out of touch with social values.

Even where there are no legal restrictions on pay levels, public opinion against high pay levels can be an important force counseling self-restraint. In 2007, for instance, it was disclosed that Wendelin Wiedeking, the CEO of Porsche AG, had earned approximately $90 million in the previous year.[369] There was a huge public outcry against this pay package.[370] This revelation may have had major policy consequences because of strong worker resentment of large pay inequities within society.[371] This example illustrates both the importance of the equalitarian norm and its limitations as a check on executive pay.

In Sweden, a strong egalitarian culture has had an important effect on CEO pay.[372] The Swedish media's intensive coverage of the "unreasonably high" levels of executive pay, and their poor connection, at certain companies led the Swedish government to set up the special committee that ultimately determined that executives' remuneration must be reasonable in relation to a company's result and growth.[373] The depth of public support for this sentiment was shown when the Confederation of Swedish Enterprise, an organization of prominent business members, stated in issuing their influential guidelines for Remuneration of Company Directors and Senior Management Personnel in 2004 that:

> The debate has chiefly centered on the remuneration of managers of the very largest listed companies, where the amounts have been considered at times to be excessive and hard to explain. In certain cases, completely unreasonable levels of remuneration have been

367. For a discussion of business culture typologies, see DERESKY, *supra* note 360, at 117–18.

368. Slade, *supra* note 363, at 23; Florence Chong, *Salary Secrets: What Companies Have to Fear*, BUS. REV. WKLY., June 5, 1987, at 50; Julie McBeth, *Who Pays the Top Salaries*, BUS. REV. WKLY., Nov. 25, 1988, at 60.

369. Mike Esterl, *In Germany, Scandals Tarnish Business Elite*, WALL ST. J., Mar. 4, 2008, at A1, A14.

370. *Id.*

371. *Id.*

372. Oxelheim & Randøy, *supra*, note 335; Peter Högfeldt, *The History and Politics of Corporate Ownership in Sweden*, *in* A HISTORY OF CORPORATE GOVERNANCE AROUND THE WORLD: FAMILY BUSINESS GROUPS TO PROFESSIONAL MANAGERS 19 (R. Morck ed., 2005).

373. Proposition [Prop.] 2005/06:186 Ersättning till ledande befattningshavare i näringslivet [Remuneration of Senior Executives in Business] [government bill], at 27, 40 (Swed.).

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> paid that—justifiably—have been condemned and that have undermined confidence in the business community.[374]

Social resistance to high pay may lead to corporate self-discipline[375] if directors suffer reputational harm when they authorize large pay packages.[376] Pay packages outside of the social norm may be more difficult for CEOs to ask for and for directors to approve.[377] If directors and managers fail to show self-control, then social pressure against high levels of income inequality may function as a catalyst for legislative reform, too. For example, the U.S. tax code was amended in 1992 to exclude deductions for managerial pay over $1 million in response to public pressure. Similarly, in the U.K. growing disquiet over executive pay motivated the U.K.'s Greenbury Committee to tackle executive pay and thereby avoid tough statutory regulation.[378] Pressures from the public could well lead to the implementation of Say on Pay legislation for the same reasons.

Cultural values can evolve as well thereby creating scope for change in executive pay practices. This certainly seems to have been the case in the U.K. Up through the 1970s, top British executives were paid less than their counterparts in all other major industrial countries,[379] perhaps because the British managerial culture was very egalitarian and U.K. firms reflected this in their pay structures.[380] However, throughout the 1980s, Britain's political scene shifted dramatically, as its ruling Conservative party espoused strong free-market ideologies. Coincident with this political and cultural shift, there were dramatic increases in executive compensation. The gross pay of CEOs in large, publicly traded U.K. firms rose nearly 600% between 1979 and 1994.[381] By the mid-1990s, British

374. CONFEDERATION OF SWEDISH ENTERPRISE, GUIDANCE FOR REMUNERATION OF COMPANY DIRECTORS AND SENIOR MANAGEMENT PERSONNEL 3 (2004).

375. BRIAN R. CHEFFINS, COMPANY LAW: THEORY, STRUCTURE AND OPERATION 699 (1997).

376. Lucian Bebchuk et al., *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751 (2002); Alex Brummer, *Failing Brakes on Boardroom Pay*, GUARDIAN, June 1, 1996, at 38.

377. Bebchuk et al., *supra* note 376. For an example of this process, see Parker-Pope, *supra* note 364, at R7.

378. CHEFFINS, *supra* note 375, at 655–56.

379. Hugh Parker, *The Effective Executive: What is He Worth?*, MCKINSEY Q. 22, 27–28 (Winter 1976).

380. CHRISTEL LANE, MANAGEMENT AND LABOUR IN EUROPE: THE INDUSTRIAL ENTERPRISE IN GERMANY, BRITAIN AND EUROPE 131–32 (1989); Andreas Budde et al., *Corporate Goals, Managerial Objectives, and Organizational Structures in British and West German Companies*, 3 ORG. STUD. 1, 27 (1982).

381. David Goodhart, *In Search of Wages that Work*, FIN. TIMES, June 27, 1994, at 14.

CEOs were among the best paid in the world.[382] This suggests that the public's willingness to implement Say on Pay legislation may change over time to reflect social views on the importance of income inequality.

D. Political Party Enacting the Legislation

Most of the countries studied in this analysis can be classified as "social democracies." While social democracies value the basic principles of capitalism and recognize its strength for producing growth and wealth,[383] they also recognize its tendency to concentrate wealth in the hands of the few. Excessive wealth concentration may hinder democracy.[384] At the same time, the social democratic state must not unnecessarily obstruct capitalism by substantially curtailing freedom of enterprise, or by the expropriation of private property in favor of the public at large, thereby jeopardizing the development and freedom of the individual.[385]

Contrary to the beliefs of communists, social democrats recognized that capitalism seemed to be able to overcome some of its major weaknesses like the exploitation of workers, unemployment and unequal distribution of wealth.[386] However, social democracy believes that capitalism needs a visible hand, and opposes too much deregulation.[387] The most famous protagonist of social democracy, Eduard Bernstein "argued that success for socialism depended not on the continued and intensifying misery of the working class but rather on eliminating that misery."[388] To this aim, "capitalism might be necessary to insure an ever-increasing economic pie, but it had to be carefully regulated by states so that its negative social and political consequences could be kept in check."[389] This regulation should balance the interests of private property with the interests of weaker parties in society. "Increasingly, social democracy adopted the goal of

382. John M. Abowd & David S. Kaplan, *Executive Compensation: Six Questions That Need Answering*, J. ECON. PERSP. Fall 1999, at 145, 146 (1999).

383. Sheri Berman, *Understanding Social Democracy*, *in* OCCASIONAL PAPERS, FRIEDRICH EBERT FOUNDATION 22 (2005).

384. FOUNDATIONS OF SOCIAL DEMOCRACIES, 58 (Tobias Gombert et al. eds., 2009).

385. *Id.* at 59.

386. *Social Democracy*, ENCYCLOPEDIA BRITANNICA, *available at* http://www.britannica.com/EBchecked/topic/551073/social-democracy (last visited July 4, 2013), *archived at* http://perma.cc/4DR2-9FLY.

387. For an analysis of party politics and ideology, see Douglas A. Irwin & Randall S. Kroszner, *Interests, Institutions, and Ideology in Securing Policy Change: The Republican Conversion to Trade Liberalization After Smoot-Hawley*, 42 J.L. & ECON. 643 (1999).

388. *Social Democracy*, ENCYCLOPEDIA BRITANNICA, *supra* note 386.

389. Berman, *supra* note 383, at 36.

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state regulation, but not state ownership, of business and industry as sufficient to further economic growth and equitable income."[390]

In countries with social democracy, the government takes into account distributional considerations of reducing excess wealth accumulation. Wealth maximization is only accepted as far as it stimulates growth and cannot be interpreted as, or even given the appearance of, exploiting any other (corporate) constituents. For many years, this underlying philosophy has dampened the level and composition of executive remuneration in countries with strong social democratic parties.

Social democracy conflicts with the typical "Berle and Means" corporation. In these firms, diffuse shareholders prefer shareholder wealth maximization and managers are encouraged to put shareholders' interests first. In corporations with dispersed ownership, managers must be made more loyal to shareholders. The corporate governance mechanisms that serve that goal are *incentivizing compensation*, hostile takeovers and transparent accounting.[391] These instruments have been underdeveloped in the continental Western European social democracies historically.

Take Germany as an example. In Germany, it was not until 1998 that the issuance of share options was legally facilitated. Hostile takeovers were highly exceptional until 2000[392] with the acquisition of Mannesmann by Vodafone and with 85% of the companies having a block-holder owning more than 25% of the shares.[393] Finally, the German accounting system diverged significantly from the US counterpart by stressing low earning volatility.[394]

Since 2000, incentive compensation, hostile takeovers and transparent accounting have become more common in most European countries. Corporate managers are heavily incentivized using stock options, the European Takeover Directive[395] has harmonized large parts of the national takeover procedures including hostile takeover bids, and the International

390. *Social Democracy*, ENCYCLOPEDIA BRITANNICA, *supra* note 386.

391. Mark J. Roe, *Political Preconditions to Separating Ownership from Corporate Control*, 53 STAN. L. REV. 539, 553–60 (2000).

392. Mayer and Franks reported three hostile bids. Julian R. Franks & Colin Mayer, *Ownership and Control of German Corporations* (Sept. 25, 2000) (Econ. Soc. Research Council, unpublished paper), *available at* http://ssrn.com/abstract=247501 *and* http://dx.doi.org/10.2139/ssrn.247501.

393. *Id.*

394. For an analysis of the differences in reporting with an application of the DaimlerChrysler case, see Ray Ball, *Corporate Governance and Financial Reporting at Daimler-Benz (DaimlerChrysler) AG: From a "Stakeholder" toward a "Shareholder Value" Model*, *in* THE ECONOMICS AND POLITICS OF ACCOUNTING: INTERNATIONAL PERSPECTIVES ON RESEARCH TRENDS, POLICY, AND PRACTICE 32–57 (Christian Leuz, Dieter Pfaff & Anthony Hopwood eds., 2004).

395. Directive 2004/25 of the European Parliament and of the Council of 21 April 2004 on Takeover Bids, 2004 O.J. (L 142) 12 (EC).

Financial Reporting Standards (IFRS) have been introduced for the consolidated accounts of stock exchange listed companies.[396] These developments went hand-in-hand with the globalization of the stock exchanges and the shift towards institutional investors' ownership.[397]

Continental European pay practices have moved toward U.S.-style practices. Since 2006, German listed companies must disclose the remuneration package of the individual management board members,[398] thereby providing employees, politicians and society easy access to information about the remuneration packages of board members of large German companies. The financial press regularly reports (indignantly) on the pay packages of top managers.[399] The number of public corporations with dispersed ownership has increased and the American-style shareholder-wealth-maximization norm has become more common.

At the same time, income inequality has increased in many Western European countries.[400] This conflicts with the basic principles of wealth distribution in social democracies. A social democratic response was needed, but straightforward mandatory executive pay caps are unacceptable because they conflict with the idea of private property in a democracy and smack of communism. A politically acceptable alternative might be to have shareholders of the locally based firms vote on executive remuneration, which will have less dramatic effects on managers' pay than direct government regulation of compensation levels. The result was Say on Pay, a "democratic" voting system for executive pay packages and/or policies.

These policies were overwhelmingly instituted by social democratic parties. This is illustrated below in Table 7, which shows the political parties that initiated the different kinds of "say on pay" in each of the five Continental European countries in our analysis. The approval of the remuneration system and remuneration report in the U.K. (2002),

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396. Regulation 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the Application of International Accounting Standards, 2002 O.J. (L 243) 1 (EC).

397. See *supra* Part II.D for further discussion.

398. Gesetzes über die Offenlegung der Vorstandsvergütungen [Vorstandsvergütungs-Offenlegungsgesetz—VorstOG] [Law about the Disclosure of the Remuneration of the Management Board], Aug. 3, 2005, GERMAN OFFICIAL JOURNAL [BGBL.] Aug. 10 2005, at 2267.

399. *See, e.g.*, Chris Bryant, *VW Adds Impetus to Executive Pay Debate*, FIN. TIMES, Mar. 12, 2012, *available at* http://www.ft.com/intl/cms/s/0/47c96cd6-6c25-11e1-8c9d-00144feab49a.html#axzz2YO3VeIT8 (last visited July 5, 2013), *archived at* http://perma.cc/9VB5-U27G.

400. According to OECD data, the Gini-coefficient increased in Germany from 0.264 in 2000 to 0.286 in 2010. The Gini-coefficient is "a standard measure of income inequality that ranges from 0 (when everybody has identical incomes) to 1 (when all income goes to only one person)." OECD, *An Overview of Growing Income Inequalities in OECD Countries: Main Findings*, *in* DIVIDED WE STAND: WHY INEQUALITY KEEPS RISING 21, 22 (2011).

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Germany (2009) and Belgium (2010) was initiated and approved by Social Democrats. In Germany, the recent unsuccessful push for a mandatory "Say on Pay" vote was initiated by the Christian Democrats preventing more harsh proposals of the social democrats. In France, the approval rules for termination agreements stem from the more liberal government in 2005 and 2007 but these approval rights are not envisaging mandatory Say on Pay. Only in the Netherlands was the Say on Pay system initiated by a Christian Democratic member of Parliament and not by the Social Democrats. In this regard, we note that the Christian Democrats are in many European countries in the middle of the political spectrum, providing legal initiatives that are welcomed by more liberal, or more socialist parties, depending on the topic and political coalitions at the moment of launching the initiative. Overall, we conclude that the Social Democrats and other left wing parties are keener to issue Say on Pay regulations.

TABLE 7: POLITICAL "WING" INTRODUCING "SAY ON PAY" LAWS

	Date	Topic	Type of Say on Pay	Introduced	Who	Political party
Belgium	April 6, 2010	Remuneration report	Advisory vote	December 2009	Government	Liberals, Christian Democrats, French speaking socialists
Netherlands	July 9, 2004	Remuneration policy	Mandatory	May 16, 2003 (via amendment)	Jan De Vries Blok Geskes	Christian Democrats
UK	July 25, 2002	The Directors' Remuneration Report Regulations 2002	Advisory vote		Government	Labour
France	July 26, 2005	Termination agreements	Mandatory	April 13, 2005	T. Breton (government)	Center right political party
France	August 1, 2007	Disclosure criteria termination agr.		June 29, 2007	government	Center right political party
Germany	July 31, 2009	Remuneration system	Advisory vote	March 17, 2009	SPD/CDU	Socialists, Christian Democrats
Germany	Pending	Remuneration system	Mandatory voting	June 26, 2013	CDU/FDP*	Christian Democrats, liberals

*overruling the far-reaching proposals of the socialists

E. State Ownership of Major Enterprises

Executive remuneration levels at companies where the government is a major shareholder in large public companies (State Owned Enterprises or "SOEs") are a politically sensitive topic in many countries. While different countries have deployed different approaches, in 2005, the OECD issued a corporate governance code for state owned entities.[401] In it, the OECD emphasized the role of the government as shareholders in setting the appropriate remuneration policies. The remuneration scheme of directors of SOEs must "foster the long term interest of the company and can attract and motivate qualified professionals."[402] The Code requires the disclosure of the remuneration policy as well as the disclosure of the remuneration levels of board members and key executives on an individual basis. The remuneration disclosure should include the termination and retirement provisions.

While the OECD Code is useful, it does not solve many of the problems facing governments in deciding what to pay SOE executives. Governments in countries with many SOEs have generally followed one of two options: direct regulation of the remuneration package of directors and/or top managers; or indirect regulation using their voting power and some kind of "say on pay." One example of direct regulation is the French cap on the total remuneration of executive directors of SOEs. The French government issued a decree in July 2012 to set the maximum remuneration of €450,000.[403] This level was said to approximate twenty times the average pay package of the lowest-paid workers at French SOEs.[404] While previously the SOEs' boards of directors determined the remuneration, subject to approval by two government ministers, the new rules forbid the Ministers from approving remuneration packages that exceed the maximum threshold.

This type of cap has indirect effects on other corporations as well. If there are no checks on pay levels at private sector firms, then the cap on remuneration for publicly listed SOEs will result in a large gap between

401. OECD, OECD GUIDELINES ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES 9 (2005).

402. *Id.* at 13.

403. Loi 2012-915 du 26 juillet 2012 relatif au contrôle de l'Etat sur les rémunérations des dirigeants d'entreprises publiques [Law 2012-915 of July 26, 2012 on the Government Control of the Remuneration of the Directors of Government Controlled Companies], J.O., July 26, 2012, p. 12283.

404. *See* Les Rémunérations des Patrons d'entreprises Publiques Plafonnées à 450 000 €, LEGIPOLE DROIT SOCIAL, http://www.droit-social-legipole.fr/les-remunerations-des-patrons-dentreprises-publiques-plafonnees-a-450-000-e (last visited July 8, 2013), *archived at* http://perma.cc/827E-V37K.

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the two sectors' executive compensation levels. This in turn will put pressure on the government to institute an indirect form of regulation by enlisting shareholders as some kind of monitors of "Say on Pay" votes on executive remuneration. As we discussed in Part I.E above, this appears to be what is happening in France today.

Belgium is a good example of a country where the government has relied on indirect regulation of SOE executive compensation via the introduction of an advisory shareholder vote on the remuneration report in 2010. This vote is applicable to both the "autonomous government undertakings" (SOEs) as well as the listed entities. This system provides more flexibility, particularly when new developments occur such as those arising at Belgacom, the largest listed Belgian SOE illustrates. In that case, only days before the general meeting of shareholders, the minister in charge opined that the remuneration of the top management of the company was too generous and the government withheld its vote at the AGM.[405] Consequently, the majority of the minority shareholders rejected the remuneration report leading the board of directors to reassess the remuneration policy of the company.

However, mandatory Say on Pay votes must be employed carefully by governments at SOEs, as the Swedish TeliaSonera case illustrates. There, the Swedish government's rejection of the company's variable remuneration based on share options caused significant renegotiation costs for all executive management contracts.[406] Ultimately, shareholders bore these additional costs.

III. PREDICTIONS ABOUT THE FUTURE OF SAY ON PAY

Having examined the different legal regimes that have been used to implement Say on Pay in many countries around the world, and analyzed the common factors that may have led to its creation in those countries, in this last Part we turn to the implications of these new rules for future of executive compensation, corporate governance, and legal doctrine. We see several areas where Say on Pay is likely to have an impact on these three important topics.

Many supporters of Say on Pay hoped that it would have a strong effect on absolute executive compensation levels, or their rate of growth.[407] The

405. *See supra* Part I.D.2 for further discussion.
406. *Id.*
407. Thomas et al., *supra* note 6.

U.S. experience suggests that their aspirations have not been realized.[408] Two studies have found that Say on Pay in 2011 had little or no impact on executive compensation levels.[409] In the U.S., this trend has continued into the early part of the 2013 proxy season.[410] Research on the U.K. has also found that overall CEO pay levels do not seem to have changed as a result of Say on Pay vote.[411]

However, a recent study of the international experience suggests otherwise. Correa and Lel use a large cross-country sample from thirty-nine countries and find that Say on Pay laws are associated with a lower level of CEO compensation.[412] They further find that the companies that are most affected are ones with poor performance. This is consistent with U.S. evidence that poor performance and high levels of pay lead third-party voting advisors to issue negative voting recommendations on their Say on Pay proposals because the companies deviate far from the average levels of all companies. Thus, abnormal levels of high pay coupled with relative bad performance trigger high levels of no votes.[413]

If these results are supported, and public pressure to rein in executive pay levels continues to mount, then we believe that a policy move to implement binding shareholder votes in Say on Pay legal regimes is plausible. The logic for such a move might run as follows: shareholders' concerns about directors being captured by management in dispersed-ownership systems, or public pressure to keep pay inequities limited, coupled with the failure to rein in increasing levels of executive compensation, means that legal rules need to increase the power of the AGM to further determine compensation policy, and define the individual packages for executives through their influence with the board's

408. Jesse Eisinger, *In Shareholder Say-on-Pay Votes, Whispers, Not Shouts*, N.Y. TIMES, June 27, 2013, at B5.

409. Cunat et al., *supra* note 39, at 5; Iliev & Vitanova, *supra* note 49 at 3. Iliev and Vitanova state: "We find that the Say-on-Pay vote had no effect on the level or the composition of CEO pay. We document no change in the ratio of equity and cash compensation as a fraction of total CEO pay, indicating that the vote had no detectable effect on the CEO compensation contract." *Id.*

410. Eisinger, *supra* note 408, at B5 (reporting that executive pay levels continue to rise steadily even after the implementation of Say on Pay); *see also* Gretchen Morgenson, *That Unstoppable Climb in CEO Pay*, N.Y. TIMES, June 30, 2013, at B1 (reporting that CEOs received a 16% median pay increase in 2012 over 2011 pay levels).

411. Martin Conyon & Graham Sadler, *Shareholders Voting and Directors' Remuneration Report legislation: Say on Pay in the UK*, 18 CORP. GOV.: AN INT'L REV. 296 (2010) (finding no change in the overall level of executive pay or its rate of growth subsequent to Say on Pay votes); *see also* Ferri & Maber, *supra* note 3, at 559 (U.K.) (finding that firms did adjust contractual features and increase sensitivity to pay for performance in response to negative vote outcomes).

412. Correa & Lel, *supra* note 5, at 2.

413. Thomas et al., *supra* note 6.

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remuneration committees. Correa and Lel find that the introduction of Say on Pay results in lower internal pay inequities within firms as well as higher firm value.[414] Most managers and directors will prefer this "internal" corporate solution to having direct regulation of executive compensation levels, such as that experienced in the financial sector during and after the financial crisis. The recent experiences in the U.K., Australia, the new European Union proposals and Switzerland, suggest that this could be a wave of the future.

We are pessimistic that Say on Pay alone will accomplish this result. To see why, it is important to remember that most companies use a benchmarking process to set their executive compensation levels: they select a group of "comparable" companies from their industry, calculate the median level of pay at those firms, and then tie pay to that median. If we remember that shareholders only vote in large numbers against the outliers in Say on Pay votes, then companies that benchmark their pay levels to the median level of firms within their industry sector are unlikely to fail their Say on Pay votes. Since the practice of benchmarking is widely acknowledged to "ratchet up" the level of executive compensation, we should not expect the growth of executive pay levels to slow until an alternative method of setting pay is adopted.[415] In other words, even binding Say on Pay by itself is unlikely to stop the growth of executive compensation.[416]

But that does not mean that Say on Pay has not had an important effect on corporate governance practices. The existing evidence strongly suggests that companies that experience significant levels of shareholder opposition against their Say on Pay proposals enhance the level of engagement between directors and shareholders.[417] This is most apparent in the dispersed-ownership companies where management now engages in much greater outreach to shareholders over compensation issues.[418] Whereas previously the shareholders were only contacted concerning votes on major transactions like mergers and acquisitions, or contested

414. Correa & Lel, *supra* note 5, at 2.

415. Charles M. Elson & Craig K. Ferrere, *Executive Superstars, Peer Groups, and Overcompensation: Cause, Effect, and Solution*, 38 J. CORP. L. 487 (2013); John Bizjak, Michael Lemmon & Thanh Nguyen, *Are All CEOs Above Average? An Empirical Analysis of Compensation Peer Groups and Pay Design*, 100 J. FIN. ECON. 538 (2011).

416. There is an important caveat to this conclusion though. If boards face other sanctions for failing their Say on Pay votes, such as those imposed in Australia's two-strike system discussed in Part I.C above, then they may be sufficiently deterred by the prospect of those consequences that they will adopt a different pay setting system.

417. Thomas et al., *supra* note 6.

418. *Id.*

board elections, shareholders are now engaged about pay packages. This represents a significant change in prior corporate governance practices that shows shareholders have greater input at many companies on pay issues.

Yet, more shareholder engagement without substantive changes to pay practices may be unsatisfying in specific situations where there is intense pressure to rein in executive pay levels. One example where such regulations have been adopted in recent years is the financial sector in the EU, and at least temporarily after the TARP legislation in the U.S., applied to bailout recipients. Another example is at SOEs in certain countries, such as France.[419] These hard-law regimes introduce pay caps, mandate certain forms of pay and directly involve governments in the boardroom on pay issues. However, we find it unlikely that these intrusive types of hard-law regulations would be introduced for other types of companies, curbing shareholder power and encumbering management.

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419. France also enacted high taxes on executive pay exceeding €1 million per year. Loi 2013-1278 du 29 décembre 2013 de finances pour 2014 [Law 2013-1278 of December 29, 2013 on the Financing of 2014], J.O., Dec. 30, 2013, p. 21829, *available at* http://www.legifrance.gouv.fr/affichTexte.do?cidTexte=JORFTEXT000028399511&categorieLien=id; *French 'Millionaire Tax' Cleared*, N.Y. TIMES (Dec. 30, 2013), at B2 (reporting that the French Constitutional Council gave the go ahead to the government's proposed 75% tax on companies awarding more than €1 million to their executives).

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