Organisation for Economic Co-operation and Development (OECD)
Corporate Governance Committee
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Submitted electronically to: CorporateGovernance&CorporateFinance@oecd.org

Subject: Public Consultation on Draft Revisions to the G20/OECD Principles of Corporate Governance

Ref: B22.18

The Hague, 21 October 2022

Dear Sir/Madam,

Eumedion welcomes the initiative of the OECD Corporate Governance Committee to publish a draft revision of the OECD Principles of Corporate Governance ('draft principles'). Eumedion is the dedicated representative of the interests of 53 institutional investors, all committed to a long term investment horizon. Together our participants invest over € 8 trillion of capital in equity and corporate non-equity instruments. Eumedion aims to promote good corporate governance and corporate sustainability at the companies our participants invest in. We consider good corporate governance and sustainability a key driver for long term value creation and for mitigating short-termism. We therefore welcome the overall direction of the draft amendments as they clearly embrace the importance of sustainability and can be expected to raise the bar for governance for companies around the globe. Please find below our suggestions to further strengthening the draft amendments.

Chapter II – The rights and equitable treatment of shareholders and key ownership functions

Principle II.C.3. General shareholder meetings in virtual or hybrid format should be allowed as a means to facilitate and reduce the costs to shareholders of participation and engagement. Such meetings should be conducted in a way to ensure equal access to information and opportunities for participation of all shareholders, regardless of whether physical or virtual. Although we welcome and encourage the use of digital tools to expand shareholder participation and

voting in shareholder meetings, we believe that the current scope of this new principle is too broad. We elaborate on this below. Currently Dutch company law does not provide for the option to hold 'virtual only' shareholder meetings and only allows for physical and hybrid shareholder meetings. Due to the Covid-19 pandemic, emergency legislation was established which provided for the option to hold 'virtual only' shareholder meetings under the condition that several requirements were met. The experiences with those virtual shareholder meetings are mixed.[1] Partly because of these experiences, the enthusiasm amongst institutional investors for holding virtual only shareholder meetings in a post corona era has waned. Therefore we are of the opinion that the scope of principle II.C.3 should be limited to a hybrid shareholder meeting model (physical ánd online participation), with also the possibility of real time, online voting. This may offer more convenience and less time commitments, allowing more institutional investors, in particular foreign institutional investors, to find their way to the shareholder meeting.

Principle II.C.5. Effective shareholder participation in key corporate governance decisions, such as the nomination and election of board members, should be facilitated. Shareholders should be able to make their views known, including through votes at shareholder meetings, on the remuneration of board members and/or key executives, as applicable. The equity component of compensation schemes for board members and employees should be subject to shareholder approval.

The consultation document suggests that independence-related information should only be reported for independent non-executive directors. However, disclosure on the reasons for which a non-executive director is classified as non-independent should also be reported.

Principle II.D Shareholders, including institutional shareholders, should be allowed to consult with each other on issues concerning their basic shareholder rights as defined in the Principles, subject to exceptions to prevent abuse.

This paragraph reads with regards to initiatives (actions) to facilitate the co-ordination of engagement activities amongst investors: *'In jurisdictions where publicly traded companies have controlling shareholders, these actions safeguard the interest of minority shareholders while increasing their voice in company matters.'* We would like to note that such actions are not only relevant for companies with controlling shareholders. They are relevant for all listed entities regardless of the shareholding structure. Considering the context of this paragraph, it could be made more explicit that sustainability-related engagement initiatives should not be considered as 'in breach of anti-competition law or as a form of acting in concert', but as an effective manner to live up to the duties of (engaged) shareholders.

Principle II.F.1 Conflicts of interest inherent in related party transactions should be addressed.

We do not support the rephrasing of 'independent' to 'non-interested' as this unduly minimises the

[1] We also refer to our evaluation of the 2020 and 2021 AGM season (https://en.eumedion.nl/clientdata/217/media/clientimages/Evaluation-AGM-season-2020-def.pdf?v=221003113443) and https://en.eumedion.nl/clientdata/217/media/clientimages/Evaluation-AGM-season-2021-DEF.pdf?v=221003113443).

role independent directors should play in the oversight of related party transactions. For instance, an executive could be non-interested with respect to a material related party transaction, yet best practice would dictate that he/she does not take part in the review and approval of such transaction.

Principle II.G. Minority shareholders should be protected from abusive actions by, or in the interest of, controlling shareholders acting either directly or indirectly, and should have effective means of redress. Abusive self-dealing should be prohibited.

We agree with principle II.G. However, we feel that the guidance on Principle II.G fails to properly achieve this. The guidance to principle II.G correctly states the following *"The potential for abuse is marked where the legal system allows, and the market accepts, controlling shareholders to exercise a level of control that does not correspond to the level of risk that they assume as owners through exploiting legal devices to separate ownership from control, such as pyramid structures or multiple voting rights"*. In several counties companies are able to allocate founders/large shareholders additional voting rights by introducing different classes of shares with different voting rights ('dual-class shares') or granting loyalty voting rights. Those structures lead to a disproportionate concentration of power for those founders/large shareholders. That power could be used to dictate the decision making process in the AGM at the expense of other shareholders. For other shareholders it will become more difficult to block decisions that negatively affect their interests or to hold board members to account. Against this background we firmly believe that shareholders' power should be proportionate to their economic interest (the so-called 'proportionality principle') and are not in in favour of granting extra voting rights to specific shareholders. We advise to reflect this position in the guidance on principle II.G in order to strengthen the protection of minority shareholders. Should the OECD nevertheless wishes to preserve the possibility of dual-class shares, we believe that safeguards should be introduced to minimise the impact of those shares. We are of the opinion that resolutions to alter the shareholding structure should be put to a separate vote, independently of other amendments of the articles of association. If the advantage to the controlling shareholder is brought about by an IPO, the supervisory board should evaluate such a shareholding structure and set out the outcome of the evaluation in its report each year. The board should ensure that the rights of minority shareholders are adequately protected (including a majority of independent supervisory or non-executive directors) and include a description of these measures in the management report. The company's articles of association must also include a sunset clause that provides for that shareholding structure to lapse automatically after a given period – three to five years. Inspiration can also be drawn from the UK listing rules on dual class share structures which entered into force on 3 December 2021 (e.g. time limit, maximum voting ratio, subjects that can be voted on and requirements with respect to the holder of the shares).[2]

Furthermore we believe that the proposed sentence under Principle II.G. *"A key underlying principle for board members who are working within the structure of a group of companies is that even though a company might be controlled by another company, the duty of loyalty for a board member is related*

[2] https://www.handbook.fca.org.uk/instrument/2021/FCA_2021_55.pdf.

to the company and all of its shareholders and not to the controlling company of the group" lacks nuance. We suggest to rephrase it to reflect that the director's primary duty in that situation is to serve the interest of the subsidiary, taking into account the interest of the parent or holding company together with the interests of any minority shareholders.

Chapter IV – Disclosure and transparency

The introduction of the chapter states that *'Disclosure requirements should not place unreasonable administrative or cost burdens on enterprises companies. Nor should companies be expected to disclose information that may endanger their competitive position unless disclosure is necessary to fully inform the investment decision and to avoid misleading the investor.'* We consider the use of the word 'may' as a too low hurdle for foregoing on reporting. In this context we consider 'would' to be more appropriate.

We support the paragraphs in Chapter III that explain how some investors engage with investee entities as a natural part of their business model. We would like this notion to be reflected in chapters IV and VI where the current references to 'investment or voting decisions' should be expanded to include 'engagement' as one of the three key investor decisions. This would also be in line with the draft General Requirements of the International Sustainability Standards Board (ISSB).

The fourth paragraph validly groups 'shareholders and potential investors'. In the context of this chapter of 'Disclosures and transparency', we see merit in making it more explicit that any reference to shareholders should be read as including potential investors as well. This would also be in line with the Conceptual Framework of the IFRS Foundation.

Principle IV.A.2. Company objectives and sustainability information.

The wording in this paragraph implies that an ESG objective is unlikely to be a commercial objective. We disagree as sustainability is getting integrated into the purposes, business models and strategies of an increasing number of companies and suggest that the phrase 'In addition to their commercial objectives,' is dropped.

Principle IV.A.3. The disclosure of capital structures, group structures and their control arrangements should be required.

We strongly agree with the added remarks on complex structures in the draft principles. We would like to add that these structures not only bring complexity for minority shareholders in certain subsidiaries; they also bring complexity to shareholders in the ultimate parent. We refer to our position paper 'Full consolidation of partly owned subsidiaries requires additional disclosure' where such complexities are discussed.[3] Investors need disclosures that help them assess the value of those parts of the fully consolidated entities that are attributable to the non-controlling interests in the group's subsidiaries.

[3] https://www.eumedion.nl/clientdata/215/media/clientimages/position_paper_full_consolidation_of_partly_owned_subsidiaries_requires_additional_disclosure.pdf?v=191119160654

Corporate bond investors need an up-to-date insight in the group structure of an entity for the continuous evaluation the creditworthiness of the parent and all the subsidiaries where debt is issued from. For decades, diagrams that provide such insight are already adequately provided in the prospectus at issuance of a bond. However, group structures tend to evolve over time and investors are in need of up-to-date characteristics of the group in the annual report. The focus of corporate bond investors on this group structure is on where the debt of the group is residing, and on what assets and guarantees are in place to support the creditworthiness of any particular subsidiary and/or bond. The text could highlight that it is important that annual reports include this information specifically for corporate bond investors.

Principle IV.A.8. Foreseeable risk factors.

The importance of this principle is diluted by the second paragraph phrasing *'is increasingly regarded as a good practice'*. We would suggest to replace the second paragraph with the following wording:

"The Principles envision the disclosure of sufficient and comprehensive information to fully inform investors and other users for each of the material and foreseeable risks of the company:

- *an accurate description of the risk;*
- *the risk appetite of the company;*
- *the nature of the risk mitigating measures and strategies of the company;*
- *the effectiveness of the risk mitigating efforts;*

The risk paragraph needs to be complemented with an incidents section that lists the key incidents that materialised in the reporting period."

A good example of this practise is the 'What still went wrong' section in the annual report of DSM N.V.[4]

Principle IV.A.9. Governance structures and policies, including the extent of compliance with national corporate governance codes or policies and the process by which they are implemented.

According to the consultation document "*Companies should clearly disclose the different roles and responsibilities of the CEO and/or chair and, where a single person combines both roles, the rationale for this arrangement*". In line with the text on p. 40 it might be worthwhile to mention that the separation of the two posts is generally regarded as good practice, as it can help to achieve an appropriate balance of power, increase accountability and improve the board's capacity for decision making independent of management.

[4] https://annualreport.dsm.com/ar2021/corporate-governance-and-risk-management/what-still-went-wrong-in-2021.html

Principle IV.A.10. Debt contracts, including the risk of non-compliance with covenants.
We suggest to replace the first paragraph with the following text that in our view more accurately describes the current practices of companies and the current needs of investors:
"Under normal circumstances, shareholders and directors control the major decisions taken by a company. However, corporate bonds and other debt contracts can contain commitments from the company that may significantly limit the discretion of management, such as covenants that restrict dividend pay-outs, prohibit the divestment of certain assets, penalise debtors if financial leverage exceeds a predetermined threshold, or trigger the immediate full repayment of the principal upon a specific breach.

As a consequence, there is a need for the timely disclosures on debt contracts: the definition and the thresholds of the most important financial covenants together with the actual performance of the company on those covenants according to these specific definitions; a description of the assets pledged to providers of financial capital, including the carrying amount of those assets on the financial position, information on any change of control clauses."

Principle IV.B. Information should be prepared and disclosed in accordance with high quality accounting and disclosure standards.
We suggest to drop 'enforceable' as the company is not responsible for the enforcement of reporting frameworks.

Principle IV.C. An annual audit should be conducted by an independent, competent and qualified, auditor in accordance with high-quality international auditing standards in order to provide an external and objective reasonable assurance to the board and shareholders that the financial statements represent fairly, in all material respects, represent the financial position and financial performance of the company.
We suggest that the first paragraph of this section introduces the long-form auditor's report as a best practice. The long-form auditor's report provides shareholders and other stakeholders with an understanding of how the auditor's opinion was formed and hence may contribute to the confidence in the audit. It sets out the materiality threshold used, the degree to which parts of the group were scoped-in to the audit and, most importantly, specifically what key audit matters the external auditor faced their underlying causes. It is critical that the auditor also explains its conclusions and to what extent this year's key audit matters were addressed, together with any unresolved issues identified in the key audit matters of the previous years.

Chapter V – The responsibilities of the board

Principle V.D.2. Reviewing and assessing risk management policies and procedures.
The principle suggests the implementation of risk committees, yet does not provide any recommendation with regards to such committee's independence, expertise, or other considerations.

We believe that additional requirements similar to those that are relevant to audit committees on independence and expertise of its members are needed.

Principle V.E. The board should be able to exercise objective independent judgement on corporate affairs.

The text was revised to specify that the designation of a lead director *"who is independent from management"* is regarded as best practice. We believe that the independence requirement should not be limited to independence from management as such director should also be independent in broader sense, in particular in relation to majority shareholders and in line with local independence best practices.

Chapter VI – Sustainability and resilience

General comments

The text of chapter VI throughout seems to imply that there is a clear distinction or even opposition between stakeholders and shareholders. The principles could make clearer that stakeholders of a company include shareholders, as well as *affected* stakeholders, such as the environment. Furthermore, responsible and engaged shareholders are focused not only on a company's financial value, but the entirety of a company's value creation and value destruction. The introduction to chapter VI could clarify this.

Though part of the chapter's title, the concept of resilience is, generally speaking, only introduced sideways. In terms of content, it seems to be primarily targeted under principles VI.C, VI.C.1 and VI.C2, though it is left largely undefined. Throughout chapter VI, the concept seems to be mostly connected to resilience to risks. We recommend to more clearly define the concept of resilience in the context of this chapter.

The introduction of this chapter starts with "Companies play a central role in our economies by creating jobs, contributing to innovation, generating wealth, and providing essential goods and services.". However this is one side of the story due to the focus on economies and not on societies and the environment in general. The paragraph could be expanded to include the notion that companies tend to cause various both positive and negative impacts on stakeholders, including the environment.

Principle VI.A Sustainability disclosure should be consistent, comparable and reliable, and include retrospective and forward-looking material information that a reasonable investor would consider important in making an investment or voting decision.

Principle VI.A.1. Sustainability information should be considered material if it can reasonably be expected to influence an investor's assessment of a company's value. If consistent with a jurisdiction's legal and disclosure requirements, such assessments may also consider sustainability matters that are critical to a company's key stakeholders or a company's

influence on non-diversifiable risks.
Principle VI.A introduces the concept of materiality in light of a *reasonable* investor's considerations regarding investment, voting decisions, and, in line with our suggestion, engagement decisions. This is a non-limitative materiality concept, which in practice includes impact materiality as well (and not only financial materiality). We strongly support this approach, which is largely in line with the approach chosen in the European Union and the draft General Requirements of the ISSB. However, principle VI.A.1 narrows the definition of material sustainability information to that which can be expected to influence an investor's assessment of a company's value (in financial terms), and includes impact materiality only in as far as jurisdictions allow such inclusion. This is inconsistent. Furthermore, principle VI.A.1 acknowledges the difficulties of assessing which sustainability information is (financially) material, which in turn should promote caution when stressing that the financial materiality of sustainability information is the most important criterium. Consistency should furthermore be created between these principles and principle VI.D.1, which introduces the concept of actual and potential adverse impacts of companies and whether these are addressed. This concept in practice goes well beyond a mere financial materiality approach.

The principle under VI.A.1 should make clear that improving corporate disclosure of sustainability information should not be (completely) dependent on investor considerations. Corporate reporting does not solely exist for use by investors and should include the notion that other stakeholders may benefit from such reporting effort as well. We recommend to remove the suggestion to limit the definition of materiality for use in corporate disclosure to financial materiality if investors in certain jurisdictions are only allowed to assess financially material information. We would support a more general acknowledgement that compliance with local laws and regulations may in some cases limit the ability of companies to adhere to the principles. It should be clear to the reader of the entire document that references throughout these principles to 'stakeholders' includes the notion that it may refer to not only existing, but also future stakeholders, thereby emphasizing the long-term nature of certain impacts and interests.

Principle VI.A.5. Phasing in of requirements should be considered for annual assurance attestations by an independent, competent and qualified assurance service provider in accordance with high quality international assurance standards in order to provide an external and objective assessment of a company's sustainability disclosure.
External assurance of sustainability information is crucial to the reliability of such information. We suggest that principle VI.A.4 as a baseline recommends high quality assurance, with phasing-in of assurance requirements positioned as a sub-principle.

Principle VI.D.1. The rights of stakeholders that are established by law or through mutual agreements are to be respected.
As suggested regarding VI.A above, we recommend creating greater consistency between principles regarding the concept of impact materiality and how it should be accounted for. VI.D.1 introduces the

concept of actual and potential adverse impacts, which is absent in the principles that concern disclosure of sustainability information.

Principle VI.D.2. Where stakeholder interests are protected by law, stakeholders should have the opportunity to obtain effective redress for violation of their rights at a reasonable cost and without excessive delay.

Where it says that effective redress for violation of stakeholders' rights should be able to be obtained at a reasonable cost, we assume this is to be understood as 'at a reasonable cost *for the affected stakeholders*'. This could be made explicit.

If you would like to discuss our views in further detail, please do not hesitate to contact us. Our contact person is Martijn Bos (martijn.bos@eumedion.nl, +31 70 2040 304).

Yours sincerely,

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