SPAIN'S CORPORATE ENTERPRISES ACT

TO INFINITY AND BEYOND

19th June 2019

The draft bill amending the Spanish Corporate Enterprises Act concluded its period of public hearing last Friday. Once the Spanish Parliament is formed, a vote on the bill will take place. If passed, it will reposition the effect of Directive (EU) 2017/828. However, some of the measures found on the draft could cause serious challenges for the market and investors. Is Spain and its business community ready for this bill? Are its measures appropriate for the functioning of the market and the protection of investors?

Given, that the draft bill concluded its period of public hearing last Friday, it is pressing that the Ministry of Economy takes into consideration the contributions made when submits the final draft to the Council of Ministers for approval. The Parliament, once it is formed, will then debate and vote the bill, introducing the amendments that it considers relevant.

The point is that the text not only includes measures likely to reposition the effects of Directive (EU) 2017/828; but goes further by including other proposals, which, according to the explanatory memorandum, have the objective for "*shareholders to participate more in the long term in the listed companies in which they invest*". In short, the aim is to minimise "*the negative impact of short-term investment strategies on the sustainable development of listed companies*".

The preliminary draft contains five points which are not included in the current directive:

1. Firstly, it establishes "*that the directors of listed companies must be natural individuals*", claiming "*reasons of transparency and good corporate governance*".

2. Secondly, it introduces "*loyalty shares*", which allow more voting rights to be granted to shareholders who have held their shares for a period of more than two years. The law states that this is "*a mechanism to encourage shareholders to maintain their investment and to reduce short-term pressures on management*", although it then specifies that it is also a matter of "*offering the same options as other European legislation*".

3. The draft bill also eliminates the obligation to issue annual financial and corporate governance reports for companies that are not originally from Spain "*reducing the disincentives to issue instruments other than shares (typically fixed income) in the country*".

4. It eliminates the "*obligation to publish quarterly financial information, which means that the Spanish standard is harmonized with practically all the countries of the EU and with all the relevant markets in Europe*" and clarifies that "*those companies that wish to continue may do so, but those that are overburdened or perceive that they are under short-term pressure do not have to*".

5. Finally, it accurately details the rules and discipline that fall under the supervision of the National Securities Market

Commission (CNMV), facilitating the work of this body and the protection of investors.

While the aim of the rule is praiseworthy, two of these five points may pose challenges to the market in the near future, and it is to be expected that in the coming months - during the parliamentary proceeding - the agents involved will present arguments to achieve a more refined balance in the final wording.

Undoubtedly, the most controversial aspect of the bill is the increase in voting rights through the instrument of "*loyalty shares*". Professor Aurelio Gurrea recently pointed out in an article that "*loyalty shares do not only contribute to the objectives intended by the Government but can, in fact, harm the financing of companies, the development of the stock market and the corporate governance of Spanish companies*". In the same text, the author indicates that in Spain "*there is neither a problem of short-termism, nor do loyalty shares contribute to the long-term involvement of shareholders, nor is the implementation of this measure considered desirable for corporate governance and the development of the securities market in Spain*".

The author states that the real reasons for this proposal are to be found on the lack of knowledge and implications of this type of shares in countries such as Spain, as well as in the tendency to "*copy-paste*" legislation from other countries "*with the desire to please certain lobbies interested in perpetuating themselves in the control of large listed companies, with the State and certain families being the most common control-shareholders in Spanish listed companies*".

In terms of quarterly results, it is worth considering the SEC's position and its interest in "*improving, or at least maintaining, investor protection through periodic disclosure of information, while reducing the administrative burden associated with quarterly reporting*". The procedure remains open and all contributions and comments can be consulted through this link, denoting the regulator's willingness to listen to all parties without forgetting its duty to protect investors and its interests in making life a little easier for companies by reducing the administrative burden.

It is difficult to determine what will happen in Spain in the coming months with this bill. Whilst everything related to the repositioning of the directive was a necessary and binding procedure under the EU directive, we must ask ourselves about the future measures and whether they are appropriate for the proper functioning of the market and the protection of investors.

Finally, and looking into the future, it seems that the SEC is also considering a formula to establish some guidelines for the use of social media by the CEOs of listed companies. The question is whether we, in Spain, want to go "*to infinity and beyond*" at this point.

Juan Rivera
+34 915 243 859
Juan.rivera@fticonsulting.com

EXPERTS WITH IMPACT™