Response of the Corporate Governance Committee of the Budapest Stock Exchange Ltd. to the Green Paper on the EU corporate governance framework

Comments in general

In our point of view, primarily the self-regulatory mechanisms shall predominate within the frame of the competitive market. Complying with the Recommendations which indicates the best market practice is a part of self-regulatory mechanisms. Compulsory rules beside this, which restrict the decision making freedom of the actors of the market (listed companies, investors) are only suggested with significant reason of protecting common interest and by taking into consideration proportionality. In the interest of the above mentioned we suggest that corporate governance shall primarily move within the frame of self-regulation and only in specially reasoned cases within the frame of state regulation.

Amongst the reasons of the Proposals short-term investor approach and the beneficial owners' distance from the company appear as problems. In our opinion, it is strongly disputable that these issues are real problems in themselves, and contributed or not to the crisis, and if yes, at which extent. Even if we suppose that the answer is yes, it is still disputable that external intervention, especially state or EU regulation is suitable for abolishing them. However, we can agree that corporate governance rules shall also react to the changed market circumstances. Although, this reaction may not mean creating additional rules, but re-consideration of the present ones. (The mentioned two new challenges are also stretch the frames of the traditional model of corporate governance owned by one significant investor (family), so the reconsideration of the basic corporate law institutes is reasonable.)

Creating additional rules and implementing compulsory provisions which eliminate the self-regulation (which support, but at least accept market diversity) can cause competitive disadvantage and significant system risks in the global market. The compulsory standardization of the solutions may transform individual risks to system risks.

List of questions

(1) Should EU corporate governance measures take into account the size of listed companies? How? Should a differentiated and proportionate regime for small and medium-sized listed companies be established? If so, are there any appropriate definitions or thresholds? If so, please suggest ways of adapting them for SMEs where appropriate when answering the questions below.

We support differentiating solutions, however the comply or explain principle still allows to differ. Besides the company size, we consider some factors also important, such as governance structure, shareholder composition, scope of activity or governance at group level.

(2) Should any corporate governance measures be taken at EU level for unlisted companies? Should the EU focus on promoting development and application of voluntary codes for non-listed companies?

Developing voluntary corporate governance codes may be supported as well, but acceptance of compulsory EU regulations is not necessary, furthermore the diversity of unlisted companies makes it difficult to evolve a unified common practice.

(3) Should the EU seek to ensure that the functions and duties of the chairperson of the board of directors and the chief executive officer are clearly divided?

The responsibilities of each committee are now defined and regulated, so it is questionable, if it adds value to define responsibilities of the executives. In our point of view, it is still recommended to retain the right of shareholders to decide upon the role of executives in a company.
If such a separation of executives may be well-founded, it should be carried out in a structure of optional task lists, that take the differences of dual and unified governance system into consideration.

(4) Should recruitment policies be more specific about the profile of directors, including the chairman, to ensure that they have the right skills and that the board is suitably diverse? If so, how could that be best achieved and at what level of governance, i.e. at national, EU or international level?

Directives can be applied in the recruitment policy, but exact instructions and numerical expectations would be difficult to define, so that it is not advisable to strive for it. Every company has the elementary aim to have an effective board of directors, having an outside influence or binding regulation is not well-founded.

(5) Should listed companies be required to disclose whether they have a diversity policy and, if so, describe its objectives and main content and regularly report on progress?

According to our opinion, the mentioned assumption goes beyond the topic of corporate governance, validation of political purposes towards diversity is not the responsibility of corporate governance regulations. EU has a different regulating opportunity in this topic. Diversity policy is the topic, where the company decides upon the public announcement of its existence, as it is considered as an important element of competitive market and business success, furthermore it is acknowledged as a value.

(6) Should listed companies be required to ensure a better gender balance on boards? If so, how?

In our point of view this assumption, like the previous ones, goes beyond the topic of corporate governance.

On an EU level, introduction of a compulsory quota or ratio is not considered necessary.

(7) Do you believe there should be a measure at EU level limiting the number of mandates a non-executive director may hold? If so, how should it be formulated?

According to our opinion, a compulsory numerical value defined on EU level, wouldn't solve the problem, but may cause administrative burdens. It seems to be more expedient to leave the companies solve this issue, since it is also the purpose of the issuers that the members of the BoD have enough time available to work for the company, even if they are in a non-executive position.

(8) Should listed companies be encouraged to conduct an external evaluation regularly (e.g. every three years)? If so, how could this be done?

In our point of view there are arguments for external evaluation, but the same amount of arguments are for internal evaluation. It should be left in the responsibility of the companies, since it has a financial impact also. We see a risk in regular, standardized external evaluations, since complying with these may get dominant, against dealing with real tasks. But without a standardized evaluation method, external evaluation doesn't bear real information.

(9) Should disclosure of remuneration policy, the annual remuneration report (a report on how the remuneration policy was implemented in the past year) and individual remuneration of executive and non-executive directors be mandatory?

We think the current regulation is sufficient, according to the corporate law it is a compulsory regulation. Not only reporting, but the decision making is also in the hand of the general meeting on the level of directives.

It can be strongly argued, to what level does the announcement by members contribute the total information providing. There are some pros, saying for making a founded investor decision the publication on a board level is satisfactory. The individual publication is rather a media event, than information for investors.

(10) Should it be mandatory to put the remuneration policy and the remuneration report to a vote by shareholders?

In Hungary the shareholders decide upon the remuneration directives, deeper operational decisions - in our opinion - shouldn't be given in the hands of shareholders.

(11) Do you agree that the board should approve and take responsibility for the company's 'risk appetite' and report it meaningfully to shareholders? Should these disclosure arrangements also include relevant key societal risks?

In case of unified and dual governing systems the tasks of BoD and Supervisory Board are separated. Concerning the banking sector, the tasks of the BoD are even more complex on the field of risk management, but decision making according to risk profiles is the responsibility of the management, the takeover of these responsibilities by the BoD is not justified.

(12) Do you agree that the board should ensure that the company's risk management arrangements are effective and commensurate with the company's risk profile?

In accordance with the above mentioned idea, the responsibilities and tasks of the management cannot be diminished by extending the tasks of the BoD.

(13) Please point to any existing EU legal rules which, in your view, may contribute to inappropriate short-termism among investors and suggest how these rules could be changed to prevent such behaviour.

In our point of view the Green Paper also does not announce that short-termism is doubtfully wrong and largely contributed to the crisis.
The question supposes that short term investor behaviour has been developed by external regulations and not because of the changing of the market. In our point of view the short term investor approach strengthened primarily not because of the external intervention, but the changed market structure. According to this, if it is justified to be eliminated at all, it would be advisable to create new rules instead of ceasing old ones.
(These new rules need complex reconsideration of the present principles, especially the one share-one vote principle and through this the equal handling of shareholders.)

(14) Are there measures to be taken, and if so, which ones, as regards the incentive structures for and performance evaluation of asset managers managing long-term institutional investors' portfolios?

We consider disputable that this question falls under the scope of corporate governance, it should be discussed under the scope of asset management regulations.

(15) Should EU law promote more effective monitoring of asset managers by institutional investors with regard to strategies, costs, trading and the extent to which asset managers engage with the investee companies? If so, how?

We consider disputable that this question falls under the scope of corporate governance, it should be discussed under the scope of asset management regulations.

(16) Should EU rules require a certain independence of the asset managers' governing body, for example from its parent company, or are other (legislative) measures needed to enhance disclosure and management of conflicts of interest?

We consider disputable that this question falls under the scope of corporate governance, it should be discussed under the scope of asset management regulations.

(17) What would be the best way for the EU to facilitate shareholder cooperation?

We think that strong reconsideration of the present rules is necessary, especially those, which helps with equal informing of the shareholders and strictly prohibit acting in concert.

(18) Should EU law require proxy advisors to be more transparent, e.g. about their analytical methods, conflicts of interest and their policy for managing them and/or whether they apply a code of conduct? If so, how can this best be achieved?

In our opinion, proxy advisor is different legal institute, so this question is not necessary to be discussed within the frame of corporate governance.

(19) Do you believe that other (legislative) measures are necessary, e.g. restrictions on the ability of proxy advisors to provide consulting services to investee companies?

In our opinion, proxy advisor is different legal institute, so this question is not necessary to be discussed within the frame of corporate governance.

(20) Do you see a need for a technical and/or legal European mechanism to help issuers identify their shareholders in order to facilitate dialogue on corporate governance issues? If so, do you believe this would also benefit cooperation between investors? Please provide details (e.g. objective(s) pursued, preferred instrument, frequency, level of detail and cost allocation).

It is supportable after getting acknowledged with the exact answers. We would like to draw the attention again that equal handling, equal informing of the shareholders and the prohibition of acting in concert can impede these forms of alternative cooperation.

(21) Do you think that minority shareholders need additional rights to represent their interests effectively in companies with controlling or dominant shareholders?

In our point of view the real problem is not that minority shareholders do not have enough rights. The more important problem is disinterest: minority shareholders do not wish to make use of these rights

(22) Do you think that minority shareholders need more protection against related party transactions? If so, what measures could be taken?

In our opinion publicity of related party transactions can do harm to the competitive condition of the company. The compulsory "independent expert opinion" about the circumstances and conditions of related party transactions can only extend the great number of similar institutions. We consider sufficient keeping the conflict of interest rules.

(23) Are there measures to be taken, and is so, which ones, to promote at EU level employee share ownership?

We can see no obstacles against that the company could decide on employee shares, but we can not see any reason for central EU regulation.

(24) Do you agree that companies departing from the recommendations of corporate governance codes should be required to provide detailed explanations for such departures and describe the alternative solutions adopted?

According to our opinion, much more exactness, more details would be important in the case of explanations, the explain option could be strengthened.
The rules of corporate governance belong to soft law, so primarily the investors should judge the quality and the quantity of the answers, how important information they are for them. However, we consider advisable to indicate the best market practice regarding the quality of the answers.

(25) Do you agree that monitoring bodies should be authorized to check the informative quality of the explanations in the corporate governance statements and require companies to complete the explanations where necessary? If yes, what exactly should be their role?

In our point of view soft law reflects the best market practice, it is part of the self-regulation of the market, so it is up to the investors to judge whether the answers to the recommendations contain enough information or not.
It is possible at present, that in case of breaching legal requirements the authority makes intervention (misleading information, failure of the publications), but the regular authority control of the reports could cease this self-regulatory feature.

Further information

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