



## 2009 Proxy Season Preview: Spain

### KEY TAKEAWAYS

Executive compensation disclosure is now receiving considerable attention in Spain as the financial crisis and new laws sharpen the focus on boardroom pay.

- As a result of Spain’s Unified Code, which was passed in 2006 and took effect in 2008, some Spanish companies have begun disclosing elements of individual director pay and have taken the step of submitting their compensation policies to an advisory vote by shareholders.
- Spain’s banks are far better off than their global counterparts, paving the way for a potential uptick in acquisition activity by major players in the country’s financial sector.
- New rules include those to give companies wider latitude with respect to buybacks.

### MARKET/REGION IN FOCUS

**Market:** Spain

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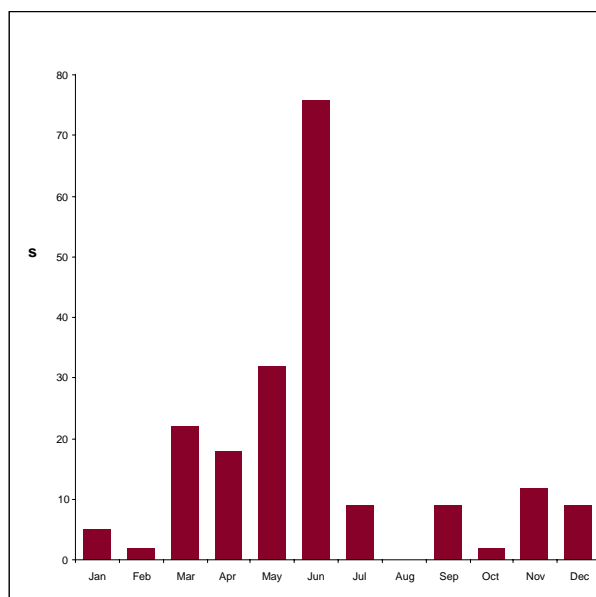
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## SPANISH SEASON PEAKS

The Spanish annual meeting season hits its peak in June. The second most popular month for annual meetings is May, followed by April. Historically, the Spanish proxy season occurred earlier in the year, though many companies have pushed back their meeting date, given that Spanish law allows for meetings to be held within six months of the close of an issuer's fiscal year, which typically is December 31.



**Fig. 1: Meetings by Month Covered in 2008**

Also of note, many major Spanish companies, including Telefonica, Banco Santander, Iberdrola Renovables, and Fomentos de Construcciones y Contratas, and Indra Sistemas, are expected to

hold their meeting in June, much as they did last year.

## ADVISORY VOTES IN SPAIN

2009 will be the second year that some Spanish companies will submit their remuneration report to an advisory vote of shareholders at their annual meeting. Recommendation 40 of the Spanish Unified Code gives wide latitude to companies with regard to pay votes, stating that compensation reports can be presented to shareholders as a separate document, or otherwise in a manner of a company's choosing.

Given the vague definition of what an advisory vote entails, and because an advisory vote is not addressed under Spanish law, most Spanish companies have opted to forgo providing investors with such a vote. Just 20 of 143 companies, or 14 percent, tracked by RiskMetrics last year provided for an advisory vote, while another five included an informational item (non-voting) on their compensation policy. Other companies, however, provided the information in a separate document without allowing for a vote.

Among these other companies are the five largest Spanish companies by market capitalization, including Telefonica, Banco Santander, Banco Bilbao Vizcaya Argentaria, Iberdrola, and Endesa. For 2009, RiskMetrics does not expect an increase in the number of pay vote proposals, based on the existing universe of coverage.

The degree to which elements of compensation are disclosed varies among companies allowing for "say on pay," with some providing a break-down between fixed and variable remuneration,

information on individual pay, and share-based compensation plans and bonuses. Other, meanwhile, simply provide aggregate compensation figures in a given category (e.g., total bonuses paid to all executives).

## CHANGES TO THE SPANISH COMPANY LAW ON STRUCTURAL MODIFICATIONS

Last month, the Spanish Government approved a new law (Ley 3/2009) affecting share buybacks, preemptive rights and other issues, following the EU Directive 2007/63/CE and a Dec. 18, 2008, ruling of the European Union Court of Justice. The law will take effect in early July, but the nature and scope of the changes may impact the coming proxy season, or, at the least, bear monitoring. Key changes are noted below.

- Increase the maximum limit for share repurchases from 5 to 10 percent for publicly listed companies over a period of 60 months, as opposed to the current 18 month holding period.
- Preemptive rights are excluded when capital is increased via non-monetary contributions.
- Preemptive rights are excluded for holders of convertible obligations from share capital increases as well as the issuance of convertible obligations.
- In relation to mergers, it is increased the level of information that should be made available to the interested parties, which shall include 1) the bylaws of the resulting entity, 2) an opinion on the impact of the merger on the industry, 3) a valuation of assets and liabilities being transferred to,

4) dates of the balance sheet accounts used to determine the share exchange ratio, and 5) potential consequences of the merger on the employment levels, types of management bodies, and the company's social responsibility.

- Eliminate the requirement to provide an external independent merger valuation if agreed to by the totality of shareholders of all parties involved.
- In the event of simple mergers, where the subsidiary is controlled by up to 90 percent, the requirement for the board and independent experts to present a report on the merger is eliminated if a reasonable compensation is offered to those shareholders of the absorbed company.
- The requirement to convene a general meeting is also eliminated when the absorbed company is controlled by up to 90 percent, unless required by holders of 1 percent of the capital.

One potential concern with regard to changes in share buyback rules concerns the change in the duration of the authority from 18 to 60 months. Eighteen months is generally viewed as a composite average under European market legislation. Although Spanish companies' practice is to renew such authorities on an annual basis thereby voiding the previous authority granted, it remains too early to assess the impact to, and reaction from, investors with regard to the new regulation.

## BANKS A MODEL IN RISK MANAGEMENT

Despite a downgrade to Spain's sovereign credit rating earlier in the year, the country's banks have proved to be in a better position than their European and American counterparts. The difference is primarily due to changes in their capital holdings, which took place nearly a decade ago, that require banks to set aside reserves based on a weighted average of their assets, with weightings determined by past default frequencies for different asset classes.

Manuel Romera, technical director for the financial sector at the Instituto de Empresa School of Business, recently noted that the reason that Spanish banks are better prepared than other banks to ride out the current financial crisis is that they have more of their own resources in proportion to assets, weighted by risk, which means they are better capitalized. "The average Spanish bank has a Basel Capital Adequacy Ratio of about 12 percent, compared with the global average of below 10 percent" Romera said. "In other words, they are handling their solvency obligations better, since they are less leveraged in their financing and have lower-risk loans."

Spain's approach is designed to smooth economic peaks and troughs by acting counter-cyclically. In practice, the rules would limit excessive growth in lending, as well as force banks to build up cushions against future losses. This means that during economic growth, the system forces banks to set aside a provision for each new loan in case it goes bad, while during downturns, banks can draw on these general provisions to cover bad loans, lessening their need to cut back on lending or raise new capital.

Although Spanish banks have avoided the solvency problems seen in the U.S. and other European countries, it is important to note that the central's bank provision has not proven effective for Spain's financial sector broadly (Spanish banks are having difficulties financing their operations), or its economy, which has fallen into recession.

For Spain's biggest banks such as Banco Santander and BBVA, the financial crisis has in fact proven to provide for acquisition opportunities, with notable purchases including U.K.-based Alliance & Leicester and Bradford & Bingley by Banco Santander, as well as Sovereign Bank, a U.S. bank, also by Banco Santander.

BBVA also completed the acquisition of two U.S. banks, Texas State Bank and Laredo National Bank, which were integrated into its wholly-owned subsidiary, Compass Bank, acquired in June 2007.

Taken together, Spanish banks would appear poised to continue seeking out opportunities for inorganic growth.

## VOTING MECHANICS

Spanish publicly listed companies (Sociedades Anonimas) must hold an annual meeting within the first six months after the company's fiscal year-end. Shareholders need to be registered at least five days prior to the meeting in order to be allowed to vote and attend the meeting. According to provisions set forth by the Ley de Transparencia of July 2003, Spanish companies must disclose all information related to the meeting at least one month before the meeting. This information should also be made available by companies on their Web Sites.

Spanish corporate law allows shareholders representing at least 5 percent of the company's outstanding common stock to request the inclusion of one or more items on the meeting agenda. To exercise that right, shareholders must submit their proposals within five days of publication of the original meeting notice. Those items proposed by a shareholder or group of shareholders must be made available 15 days prior to the meeting. Also of note, some Spanish companies require shareholders to hold a minimum number of shares in order to attend the meeting, and shareholders may be represented at the meeting by a proxy, who need not be a shareholder, per requirements set under a company's bylaws.

Spanish law allows shareholders to cast their votes via mail or by electronic means. Shareholders wishing to cast their votes electronically should present an electronic certificate with a valid electronic signature issued by the Autoridad Publica de Certificacion Espanola (CERES) in order to guarantee the security and authenticity of votes cast electronically.



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