

To Bank Shareholders

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Bank Investors Campaign – Update No. 16 – Lloyds Bank

Lloyds Bank

The day after we issued the last newsletter, which suggested that shareholders should vote against the re-election of Sir Victor Blank at the forthcoming Annual General Meeting (AGM) on the 5th June, he announced he was going to step down before the next AGM in a year's time. Whether our suggestion prompted this, or he came under strong pressure from other quarters to go is not known. The support of UKFI, who would be voting the Government's 43% stake, seemed unclear so it looks like this is a face-saving compromise where he can depart gracefully rather than being ejected by a vote. We issued this press release on the day he announced his resignation: www.uksa.org.uk/UKSA_Press082_Lloyds_Voting.pdf

Does this affect our recommendation? The answer is NO. We see no reason for Sir Victor to stick around for another year and collect another year's salary. We cannot see any justification for accepting this "compromise". There are other non-executive directors on the board who can take over as Chairman temporarily while a new one is found.

Note that no details of the terms of his departure or any financial compensation have been disclosed but we would oppose any pay-off because failure should not be rewarded (and the HBOS merger has clearly been a massive strategic error for which the Chairman must be accountable).

Incidentally Manifest, the Proxy Voting Agency, have a blog which recently suggested that the directors of Lloyds TSB might have breached their duties under the Companies Act. They said: "*Irrespective of the political pressures surrounding the transaction at the time, Daniels' admission [of limited due diligence] raises fundamental questions in our mind as to whether the directors' actions would meet the objective test set out by Hoffman J. in Norman v Theodore Goddard [1991], i.e. that an assessment of what the director should have done or known is to be based on what 'a reasonably diligent person having both (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company and (b) the general knowledge, skill and experience that the director has.'*"

More information at <http://blog.manifest.co.uk/?p=935>

Lloyds AGM

Several of our committee are planning to attend the Annual General Meeting with the intention of asking questions and we may be organising some supporting events for our contacts. If you plan to attend the AGM in Glasgow and would be willing to assist then please give me a call on 020-8467-2686.

Placing and Compensatory Offer

Lloyds Banking Group shareholders should also have received a voting form for the proposed share placing which is to be voted on at a general meeting immediately after the AGM. This share placing is as originally announced, i.e. shareholders can subscribe for 0.6213 new shares for every one share they hold at a price of 38.43 pence (a substantial discount to the current share price), but with one difference. The change is that instead of an "excess subscription" facility being provided to wipe up those shares not subscribed for, any shares not subscribed for will now be sold in the market and the proceeds given to those shareholders who did not take up the offer.

This seems a good change as it will at least provide some compensation to smaller shareholders who are so strapped for cash that they cannot take up the offer.

Note that we cannot give you investment advice as to whether you should take up these shares or not, for legal reasons. There may be some general advice given in the national newspapers, but it probably depends on whether you wish to acquire more shares in the company, your general view of the prospects for Lloyds, and whether you have the cash to do so.

Should one vote to approve the share placing? The justification given for this placing is to strengthen significantly the company's tier 1 capital ratio position. In addition the company is redeeming the Preference Shares issued to HM Treasury, which may enable it to start paying dividends again (although there is no prospect of that in the short term), and will remove the costly dividends paid on those preference shares. Originally this placing was also linked to involvement in the Government's Asset Protection Scheme to insure the toxic assets of this and other banks – but Lloyds is still negotiating the terms of that deal. So now we are voting on the share placing alone.

The issue of more equity at a low price to enable redemption of the preference shares does however mean that the Government effectively converts its preference shares to a very large equity stake at a very low cost and this was not anticipated in the original preference share fund raising. In addition, shareholders need more details of the Asset Protection Scheme which have not been provided, to be able to judge the future prospects of the company and the need for such funding. We therefore recommend voting against the placing.

Brussels Intervention

One ominous warning in the Placing document is that the European Commission will have to give clearance to the Asset Protection Scheme. Some analysts have commentated that the Commission might require significant restructuring, even down-sizing of the company to avoid any suggestion of state aid. The Government's original waiving of Competition Law may come home to haunt it if that is the case as it will undermine one of the few positive arguments for the merger – that "size" can help.

Campaign News

The Committee we have formed to tackle the Banking Crisis is splitting into two:

a - One will be a "Lloyds Shareholder Action Group Committee" and will deal with the legal issues and past events at Lloyds Bank, with a view to trying to obtain some restitution for shareholders damaged by the events at that company. This committee will be chaired by Nick Shaw.

b - The other will be a "Bank Policy Committee" and will deal with the political, regulatory and other aspects that have impacted banks and their shareholders with the intention of getting improvements going forward. I will chair this committee, at least temporarily.

The latter might cover such things as representations to the Walker Review on Remuneration where we expect to make a submission.

There will as a result be two separate newsletters going forward, and we will try to ensure that shareholders in specific companies only receive the specific company newsletter, but all bank shareholders will receive the "Policy" one which may be less frequent.

At least that's the plan although it may take some time to execute.

As regards the Lloyds Shareholders Action Group, we do now have the share register and are intending to write to as many shareholders as we can as soon as possible. The legal issues are still being worked on.

Treasury Committee

The House of Commons Treasury Committee recently published its latest report on the Banking Crisis which is an analysis of Corporate Governance and Pay in the City – available in full from www.publications.parliament.uk/pa/cm/cmtreasy.htm .

They rightly say that the advisory vote on companies' remuneration reports, in place since 2002, has largely failed to provide an effective check on remuneration levels and policies. They suggest remuneration committees would benefit from having a wider range of inputs from interested stakeholders which seems difficult to dispute. At present a coterie of non-executives determine remuneration policies, supported by remuneration consultants, and this combination simply results in a consistent ratcheting upwards of pay.

They rightly point out that non-executives have failed to act as an effective check on the executive managers in banks, and question whether their role and experience need to be reviewed. Many seemed to lack relevant experience in a very complex environment, and others simply did not dedicate enough time to the job.

As usual whenever companies are seen to be going wrong, the phenomenon of "ownerless corporations" is raised. The vast majority of institutional fund managers, who now control most shares, have no ownership interest and the real "beneficial owners" have no say.

They certainly believe that poorly structured remuneration policies contributed to the banking crisis by encouraging risky behaviour among directors and managers. They have produced quite a few detailed recommendations, and also ask that the Walker Review attack some of these issues specifically. But they question whether Sir David Walker has the right background as a City insider to be the ideal person to take on this task.

For those interested in remuneration issues, it's well worth reading the full report.

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Note that all previous information issued by UKSA in respect of our campaign on banks is present on the following web site page: www.uksa.org.uk/Bank_Investors_Campaign.htm