

Company Law Reform Bill – Summary of the Existing Defects and Proposed Amendments re Shareholder Enfranchisement

1. What is Wrong With the Bill as Regards Shareholder Enfranchisement?

The UK Shareholders Association originally expressed support for the proposals on shareholder rights for nominee accounts as outlined by the European Securities Forum (ESF) and supported by the Company Law Reform White Paper. The latter assumed that the financial services industry would voluntarily adopt a comprehensive system to implement such enfranchisement if “enabling” legislation was introduced. But it is clear from the discussions at the Shareholder Rights Working Party (a body representing many financial industry participants) that there is no unanimity about how such a system might operate, or indeed wide support for a general implementation.

It has clearly been a major concern of our members that shareholders in nominee accounts are generally ill informed, and lose the basic rights enjoyed by shareholders whose names are on the share register. Such rights are the ability to vote at general meetings of the company, to attend and speak at such meetings and to request resolutions.

Unfortunately with PEP and ISA holders being forced to use nominee accounts, and stockbrokers and issuers generally promoting such nominee accounts for new shareholders, many private shareholders have lost their basic rights, and the new Bill is not going to solve this problem in a comprehensive way. As many as 10 million people in the UK who hold shares in this way are therefore effectively disenfranchised, and the provisions in the new Bill are unlikely to change that for most of them.

The defects in the Bill as introduced to Parliament are:

a. Only Optional for Companies. The Bill relies on the voluntary support of Companies to change their Articles to support enfranchisement of nominee shareholders in full. However, it is clear from the comments of such parties as the CBI and QCA (the latter representing smaller quoted companies) that many companies are unenthusiastic about implementing such enfranchisement, primarily based on their concerns about costs, even though they will be making substantial savings from the use of electronic communication to their shareholders as supported by other aspects of the Bill.

b. Reserve Powers Only Cover Provision of Information. Although the Bill contains reserve powers in Part 9 Clause 137 to enable the Secretary of State to compel companies to provide information to shareholders in nominee accounts, there is no provision to compel the provision of voting or other rights. Full shareholder enfranchisement requires a lot more than the simple provision of information to shareholders and in reality such information is already freely available anyway.

Even if and when brought into operation by the Secretary of State, the existing wording of the Bill would at best provide little extra benefit to shareholders. What they really need to be enfranchised is not being guaranteed at all.

c. Also Only Optional for Stockbrokers. In addition for shareholders to be enfranchised, the nominee operators (i.e. Stockbrokers) must support those companies who have selected to enfranchise their nominee shareholders. If brokers are not willing to supply the names and addresses of their nominee shareholders to the companies and their registrars, then companies cannot send them information. Similarly they must either vote on behalf of the shareholders, or pass those voting rights on to the shareholders. But there is no compulsion for nominee operators to do any of these things under the Bill, and it is clear that many brokers see no need to do so, or have objections to doing so on cost or other grounds.

d. Will Result In Patchy and Unclear Implementation. In practice, with half-hearted commitments from many companies, and from many stockbrokers, implementation of shareholder enfranchisement will be patchy at best. Individual shareholders may find that if they hold a number of shares in a nominee account portfolio, only some of them might provide enfranchisement, and it may not even be easy for the shareholder to determine which ones are doing so. Also, some companies may provide some rights but not others, so again an individual shareholder will not be clear as to what rights he has in any particular case. Simply on the grounds of practicality and clarity for shareholders, the Bill needs significant revision.

e. Summary. In summary we have a proposed system which is probably going to have little take-up by brokers, is unenthusiastically supported by companies and in which registrars have no interest (except to minimise their own expenditure of effort in supporting the system). Perhaps it's not surprising there has been no unanimity on how it should operate!

We are therefore proposing that the provisions of the Company Law Reform Bill as regards shareholder enfranchisement are considerably strengthened so that the Government provides the necessary leadership to the financial services industry on this matter.

2. Shareholder Enfranchisement Should be Comprehensive but Take-Up Optional

Note that we are not proposing that shareholders be enfranchised or receive information if they don't want to do so. Many shareholders in nominee accounts are happy to rely on their advisers to operate the account and select investments. Beneficial shareholders will need to be able to opt out if they wish - this might apply for example to those shareholders whose holdings are managed on a discretionary basis, or they wish to be in a "blind" trust. Our proposed amendments therefore only provide any compulsion where a shareholder specifically requests to be enfranchised (stockbrokers would be able to say that for certain types of accounts, their clients must agree not to submit such requests).

3. Our Proposed Amendments

The principles behind our proposed amendments to the Bill are:

a. All Rights, Not Just Information. We propose that the powers of the Secretary of State to require companies to enfranchise shareholders should cover all rights applicable to normal members of the company, and not just the provision of information.

b. A Clear Implementation Process and Timetable. We propose that the Secretary of State has a duty to publish a timetable for implementation of the above powers for all listed companies within one year of the Bill becoming law, after consultation with financial industry participants. This timetable would lay down what classes of companies might be included at each stage as we accept that some companies may find it easier to comply than others.

c. A Clear Obligation on Stockbrokers to Support Enfranchisement. We are proposing that nominee account operators have an obligation to provide the necessary information to companies about the beneficial owners of the shares to enable the companies to enfranchise them, subject to the request of those shareholders. But nominee operators would be able to exclude such requests if they had originally specified in their contract with the client that no such obligation would exist – this would cover those types of accounts where the beneficial shareholder did not wish to have such rights (but the form and wording of such contracts would be subject to regulation so that it was clear to shareholders that they were giving up such rights).

d. Rights to be Enforceable in Law. We suggest that the rights granted to nominee shareholders by the Bill are enforceable against the company (we see no reason why they should not be).

Note that we are not proposing to incorporate into the Bill any details of how enfranchisement will operate in practice, i.e. the proposals would still only be “enabling” legislation in that it will still be up to the financial services industry, companies and brokers to develop systems to support the principles of enfranchisement embodied in the Bill. The Secretary of State would also have discretion about the nature and timing of the regulations to implement the provisions of the Bill, and would be required to consult the financial services industry about the details of the regulations.

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