

To all UKSA Members

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UKSA Criticises the Company Law Reform Bill and Asks for Your Support to Strengthen the Provisions on Shareholder Enfranchisement

The new Company Law Reform Bill has recently been introduced into the House of Lords. The UK Shareholders Association welcomes many provisions of the Bill but feel that the provisions for the enfranchisement of nominee shareholders are totally inadequate.

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. 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. **But it is now clear to us that without more vigorous Government intervention in this matter, no satisfactory solution is likely to appear and the provisions of the Company Law Reform Bill are simply not strong enough. Here's a chance for you to support UKSA and we are asking you to write to your Member of Parliament on this subject.**

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.

What We May Get

The solution that has been developed and is supported by the new Bill has the following primary features:

A – Companies may amend their Articles to support governance (e.g. voting rights), but this is optional, and it seems quite likely that many if not most, will not do so.

B – It is not even clear whether companies will have an obligation to provide information such as the Annual Reports & Accounts in electronic form as this requirement is only embodied in a reserve power of the Government in the new Bill. There is no commitment to use this power at all, and it does not even provide a right enforceable in law by shareholders.

C – The Company Law Reform Bill proposes that companies can choose which rights they actually offer such indirect shareholders, so that some companies might choose to offer just information, others may offer voting rights but not rights such as the ability to call for an EGM, while yet others might offer full rights. It is up to the companies to choose which rights, if any, they give beneficial shareholders by changes to their Articles.

D – In addition, it will be optional for brokers and/or other operators of nominee accounts to support the Companies in the provision of such rights to their beneficial shareholders. Indeed only certain brokers seem to have much interest in this, while other brokers suggest they already have adequate facilities, for which there is no demand anyway. However, it is clear that any brokers offering such facilities will be likely to make some extra charge to cover their own additional costs of providing such information or supporting voting systems.

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!

In addition, brokers expect to incur costs in implementing any solution which they will pass on to the shareholders, instead of the issuers taking on that liability in full. This will discourage take-up of the facility by brokers' customers.

Exercising Voting Rights

One proposal that has been made is that the exercising of voting rights should continue to be handled by nominee account operators (eg. stockbrokers), who would aggregate their beneficial holders' instructions. In reality, separating the flow of information from the company to the investor, from the return of voting instructions seems odd to say the least, and will lead to enormous practical difficulties, as it does at present for those brokers who attempt to support such a system. Will all beneficial shareholders know when to vote, and what they might be voting about? Will brokers actually pass on the required voting instructions to their clients in a timely and reliable manner?

Shareholders Will Not Be Clear on their Rights

Because different companies may or may not enfranchise shareholders, and may indeed provide different levels of support for various rights, and brokers might also offer different levels of support, it will be totally confusing as to what rights an indirect shareholder might receive. Is a shareholder, who might have many shares in his portfolio, really expected to keep track of what rights he might or might not have in each? As a registered shareholder you always know what you should be receiving, and can easily double check for any missing notice of a General Meeting. But that will not be the case for indirect shareholders. In essence, the proposed system will simply be a mess.

Compare that with the US system where all indirect shareholders receive all information from all their investments as a matter of right, and also receive any required proxy voting forms in the same way. In essence, a simple yet comprehensive system that operates in the best interest of shareholders rather than the industry service providers and the issuing companies.

Note that we are not proposing that shareholders be enfranchised or receive information if they don't want to do so. Beneficial shareholders would be able to opt out if they wished - this might apply for example to those shareholders whose holdings are managed on a discretionary basis.

Over Complex and Impractical Solutions Instead of a Simple Principle

Unfortunately no agreement has been reached on how to enfranchise shareholders and most of the proposals have been complex to implement and not comprehensive. Indeed what we suggested in our comments on the Company Law Reform White Paper were "We are not clear why the chosen route towards enfranchisement is the complicated one of (partially) enabling nominees to assign 'all or any specified rights', instead of the more direct route of legislating that the beneficial holders through the nominee accounts of registered brokers are ipso facto enfranchised, with all the rights of an on-the-register shareholder".

We see no reason why such indirect shareholders should not simply be recorded on the share register as additional members in the same way as "designated" nominees are, and it does not seem to us to be beyond the capabilities of modern technology to support such a system at no significant additional cost.

But clearly one difficulty is the lack of any enforcement or encouragement in the Company Law Reform Bill to persuade brokers and issuers to participate in such a scheme. The proposed changes to Company Law, which appear to have been designed purely to facilitate an agreed industry or market-based solution, will in practice not be sufficient with the existing attitudes of industry participants to effect any substantial change and ensure most indirect shareholders are enfranchised in a reasonable time frame.

How You Can Support the UKSA Campaign

I cannot emphasise too much how important it is that we get some changes made to the Company Law Reform Bill, as otherwise it is likely to be many years before this issue is revisited. You can personally help by writing to your MP, and to anyone you know who sits in the House of Lords, on this issue.

A suggested letter you might use as a template follows, but please use your own words and rewrite it if possible so as to avoid it looking like a straight copy. Please do this today as it is urgent to bring this to the attention of politicians!

Yours sincerely

David Blundell
Chairman

Note: More information on this issue and copies of this letter in digital format are present on our web site at www.uksa.org.uk/Company_Law.htm , or call the main UKSA number above if you have any questions. If you do not know who your MP is then either call UKSA or go to the following web site: www.locata.co.uk/commons

To: _____
Member of Parliament
The House of Commons
London
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Dear Mr _____,

As you may be aware, the new Company Law Reform Bill has recently been introduced into Parliament. Although there are many good aspects of this bill, I would like to bring to your attention a major deficiency in this proposed legislation. Namely that it will not enfranchise those shareholders who hold their shares in nominee accounts.

Although the previous White Paper referred to the extension of "governance rights" to indirect investors in companies, and the "right to information", in practice what we are likely to get as a result of the Bill is a system that will be optional for companies, optional for nominee account operators (e.g. brokers) and complex to understand for shareholders.

Instead of a clear commitment by the Government to enforce proper legal rights for beneficial shareholders at best we have a weak commitment at the whim of the Secretary of State to get just information supplied to such shareholders. There is no commitment to ensure voting or other rights, and the lack of a Government lead to the financial industry will result in a patchy, half-hearted system at best. Compare that with other jurisdictions such as the USA where all shareholders have the same rights as a matter of law.

Note that I am a member of the UK Shareholders Association, who represent the interests of private shareholders, and more information on this subject is available on their web site at: www.uksa.org.uk/Company_Law.htm.

Could I ask you to look into this matter, and take up the issue with the relevant people in the Government and in your own party, as it is surely of major concern to those millions of people who hold company shares, particularly those with PEPs and ISAs who are forced into nominee accounts by the Government's own rules.

Yours sincerely
