

Press Release

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Walker Review Misses The Governance Point

UKSA Proposals To Introduce Real Change

The UK Shareholders Association (UKSA) comments that, as expected, the Walker Review recognises that institutional shareholders have little reason to care about governance issues and wants to change this. But it fails to get to the heart of the matter.

Weakness of Review Proposals

Sir David's proposals on governance ⁽¹⁾ amount to exhortations to the institutions to try harder. This is a pity when his Review contains an excellent analysis of the reasons why this would be ineffective ⁽²⁾.

Institutional shareholders fail to exert the necessary ownership interest over banks (and over quoted companies in general) because the money invested isn't their own. They are agents for millions of individual savers ⁽³⁾, but those savers, whose interests are, in the main, long term and governed by prudence, don't have a voice.

The Review also discloses disturbing failures in the mechanics of share voting which suggest that the Exchange systems are designed more for the benefit of participants than the exercise of shareholder democracy ⁽⁴⁾.

UKSA's Proposals

UKSA makes the following proposals:

- The fact that large numbers of individual investors who invest via nominee accounts (which includes all investors in shares within ISAs and SIPPs) are disenfranchised ⁽⁵⁾ should be treated as the scandal that it is, which requires real political will to resolve.
- The Treasury should bring forward proposals to give a voice to non-institutional beneficial owners of shares, including individuals, trustees and smaller wealth funds. A starting point already exists in the Protection of Shareholders Bill ⁽⁶⁾ presented to Parliament earlier this year.
- The FSA should investigate, and report on, stock management practices that lead to beneficial investors being denied the vote to which they are entitled. This would be a necessary preliminary to a debate on what those practices should be.

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Until companies are brought under the control of those whose interests are tied to long-term wealth creation, we can expect a continuation of recent practices of excessive risk-taking, over-leveraging, volatility, ill-judged takeovers and the wealth destruction that goes with it ⁽⁷⁾ .

Notes for editors:

(1) The Review makes nine recommendations on governance: two involve closer monitoring of the share register, five involve tinkering with the already existing Statement of Principles governing institutional behaviour, one suggests the creation of a 'Memorandum of Understanding' between 'major long-only investors' and one concerns disclosure of voting policies.

(2) The Review identifies the following impediments to effective institutional engagement with companies (paras 5.17/18):

- The effective governance of companies requires too much time and expense.
- Those who don't engage ride freely on the backs of those who do.
-which nevertheless delivers no advantage when a fund's performance is measured against a benchmark.
- There are worries about maintaining confidentiality.
- Confrontation could damage commercial relationships.
- There may be legal barriers to concerted shareholder action (concert party rules).
- Voting against a board can have little effect (unless concerted) and may reduce subsequent access.
- Voting against a board can damage the stock price, contrary to a manager's fiduciary duty.

(3) Note (2) above lists the problems of getting institutions to engage at all. The obstacles to getting them to engage sensibly - summarised as 'the agency problem' (paragraphs 1.11/12) and the 'conflict of interest problem' (note (7) below) are another matter again.

(4) The Review lists the following 'voting impediments' (para 5.17): cross-border voting restrictions, short notice periods, share blocking, bunching of items and custodian practices. Annex 6 of the Review illustrates the disturbing lack of information on the ownership of equities in the UK.

(5) The Companies Act 2006 established a framework which enabled shareholders in nominee accounts to be enfranchised, giving them the right to vote. It has been ineffective, mainly because most stockbrokers who manage the nominee accounts have not taken it up.

(6) The Protection of Shareholders Bill proposes Shareholders Committees to engage with companies on behalf of individual shareholders.

(7) There are potential conflicts of interest inherent in the diversified activities of financial conglomerates of which fund management is usually a part. Stockbroking, trading, underwriting and particularly investment banking benefit from volatility and 'deal flow' but not necessarily from the unspectacular devotion to the basics of good business that characterises well-managed wealth creation.

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About the UK Shareholders Association (UKSA)

UKSA is the leading independent organisation which represents the interests of private shareholders in the United Kingdom. We campaign to protect the rights of shareholders in public companies, and to promote improved standards of corporate governance. Our educational activities, regular regional meetings, company "analyst" meetings and the resources of our web site, help to inform the public on investment management. UKSA is a "not for profit" organisation which is financially supported primarily by its individual members.