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Dear Sirs

Walker Review – Shareholder engagement and change in control requirements under the EU Acquisitions Directive

This is a response from the Regulatory Committee of the City of London Law Society to the Walker Review.

The City of London Law Society is the local Law Society of the City of London and represents City solicitors, who make up 15% of the profession in England and Wales. Members of the Regulatory Committee advise a wide range of firms in the financial markets including banks, brokers, investment advisers, investment managers, custodians, private equity and other specialist fund managers as well as market infrastructure providers such as the operators of trading, clearing and settlement systems.

The Walker report dated 16 July 2009 (the "Report") calls for greater engagement by shareholders with the Boards of financial institutions "with the aim of supporting long-term improvement in performance" (see Executive Summary, page 9). In this regard it highlights the importance of collaboration with other shareholders on matters of shared concern (see paragraph 5.42).

The Report also notes at paragraph 5.44 possible constraints placed on this type of collective shareholder action by the controller regime contained in Part XII of the Financial Services and Markets Act 2000 ("FSMA"). In particular, recent amendments to this regime on implementation of the EU Acquisitions Directive (the "Directive") have extended the requirement to notify proposed acquisitions of shares in a regulated financial institution to persons who are "acting in concert". The term "acting in concert" is not defined in FSMA, but guidance on its meaning (the "Guidance") published by the three Level 3 Committees (CEBS, CEIOPS and CESR) is drafted in extremely wide terms. Based on the Guidance, we share the concern of others that shareholder collaboration of the kind recommended by the Report may bring those shareholders within the controller regime even though their activities are not linked to the acquisition of shares or voting power in the relevant regulated financial institution.

Because of this, we welcome confirmation from the Financial Services Authority ("FSA") in a letter dated 19 August 2009 to the chairman of the Institutional Shareholders Committee that "ad hoc discussions and understandings in good faith solely aimed at exerting influence intended to promote generally accepted principles of good corporate governance" are not intended to be captured by the phrase "acting in concert" as used in the Directive, FSMA or the Guidance and that the FSA will apply this approach under the controller regime in Part XII of FSMA. We believe this approach is consistent with the wording and objective of the Directive. However:

- The precise scope of the Guidance remains unclear. In particular, it is not clear that supervisors in other EEA Member States are in agreement with the FSA's approach, which may be particularly relevant on changes in control relating to financial groups where there are regulated subsidiaries throughout the EEA.

- The FSA's wording (in quotes above) leaves scope for argument about whether proposed action is "solely aimed at exerting influence intended to promote generally accepted principles of good corporate governance". It is not difficult to see that a Board's view of principles of good corporate governance might differ from that of its shareholders. Further, the FSA's comments are limited to the promotion of good corporate governance and will not cover any attempt by shareholders to influence Board decisions in other respects, including in relation to corporate activity.

These issues will remain a problem while the Guidance remains in its current form. We would therefore encourage the FSA to support a review of the Guidance, with a view to achieving agreement among EEA Member States about the types of shareholder activity that can be carried out without concern about triggering notification requirements under the Directive.

There are strong arguments, in any case, why the Guidance is inconsistent with the terms of the Directive. For example, Recital (1) of the Directive states that controller requirements "regulate situations in which a natural or legal person has taken a decision to acquire or increase a qualifying holding in a [financial institution]". Similarly, the requirements of the Directive are triggered when a person or persons acting in concert "have taken a decision either to acquire ... a qualifying holding in [a regulated firm] or to further increase ... such a qualifying holding ...". This suggests that the Directive is intended to cover situations involving the concerted acquisition of shares by two or more investors rather than situations where those investors decide only to vote together on a particular issue.

In the light of this, and given the Report's recommendations concerning shareholder engagement, we would very much welcome the support of the FSA and HM Treasury in initiating a review of the current form of the Guidance.

We would be delighted to discuss the above concerns with you. You may contact me on +44 207 295 3233 or by e-mail at margaret.chamberlain@traverssmith.com.

Yours faithfully

Margaret Chamberlain

Margaret Chamberlain
Chair CLLS Regulatory Committee

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