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City of London Law Society Company Law Sub-Committee response to the Kay Review of UK Equity Markets and Long-Term Decision Making

The City of London Law Society ("CLLS") represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees and in this case the response has been prepared by a working party of the CLLS Company Law Sub-Committee comprising senior and specialist corporate lawyers. Our comments below are made with reference to the numbered questions in the call for evidence paper. We have chosen only to answer three questions as the others we consider are better addressed by others.

Question 1: Whether the timescales considered by boards and senior management in evaluating corporate risks and opportunities, and by institutional shareholders and asset managers in making investment and governance decisions, match the time horizons of the underlying beneficiaries.

We do not seek to answer the question as such, but we do wish to note that layers of corporate ownership can be numerous and complex. It can therefore be difficult to identify a company's true beneficial shareholders (and those ultimately economically funding the investment) and, in turn, their underlying interests, whether short or long-term. As a simplistic example, a pension investor's interests aged 35 are quite different from their interests aged 60, and the degree to which the advantages or disadvantages of passing decision taking powers to intermediate managers with expertise outweighs the disadvantages of potential mis-alignment of timing objectives which can result, is a conceptual debate which it is not for us to comment on.

Question 3: Whether the current functioning of equity markets gives sufficient encouragement to boards to focus on the long-term development of their business.

We believe that directors of public companies generally recognise and take seriously the need to focus on the long-term development of businesses. Our experience is that, in practice, boards do frequently take long-term factors and implications into account as part of their decision-making. Indeed, the statutory expression of the fiduciary duty of directors "to promote the success of the company" includes a requirement for directors to "have regard (amongst other matters) to the likely consequences of any decision in the long-term". However, we would not suggest that board consideration of long-term issues arises or has improved as a result of the statutory duty, rather it arises more from the desire of directors to fulfil their duties in the relevant company's best interests both responsibly and well.

We think it is essential that there should be a good empirical basis to support any introduction of additional obligations on companies and their directors. Given our view that long-term considerations are already taken into account by boards and the limited impact of the relatively new statutory duties, we are concerned that any additional legal obligations imposed on companies and directors in this regard will be of little benefit to ultimate investors in practice.

In our response to the call for evidence from the Department for Business, Innovation and Skills on the existence of short-termism and market failures in the UK equity markets, we raised a concern that the UK disclosure regime for listed companies can inhibit forward-looking and long-term disclosure. We do not repeat all of the points in this response but we do think that increased disclosure of long-term objectives and issues may facilitate a more open debate and increased focus on long-term development and strategy.

Question 7: Whether there is sufficient transparency in the activities of fund managers, clients and their advisors, and companies themselves, and in the relationships between them.

As a general observation, we believe that transparency at the level of public company ownership and activities has improved over recent years in part because of legislative intervention. The application of the Stewardship Code should also enhance transparency as reporting develops in accordance with its principles.

In relation to the existing rules on disclosure of material stakes in public companies, in our view, the combination of the powers of boards to require those who have an interest in the company's shares to provide information about themselves under Part 22 of the Companies Act 2006 and the disclosure regime under chapter 5 of the Disclosure and Transparency Rules ("DTRs"), which requires the proactive disclosure by shareholders whose interests represent 3% or more of the votes exercisable at general meetings, provide public companies with the ability to obtain the information they require on the identities of their principal shareholders. That is supported by the additional disclosures required of investors in companies subject to takeover offers.

We note that the existing regime under the DTRs requires disclosure of a broad range of interests in shares (in addition to beneficial owners holding shares through nominees, the interests that must be disclosed include interests arising from agreements to acquire shares, derivatives that relate to the shares and entitlements to deal with voting rights). We do not see any reason to change this regime (for example, by reducing the threshold for disclosure), which is now reasonably well understood. Any change would have cost implications for investors, which would have to be balanced against any benefit that was perceived to be gained from a change. The balance between further transparency of holdings on the one hand and the cost and burden of more disclosure on the other has recently been extensively considered by both the Takeover Panel and the FSA, as they have reviewed the relevant disclosure regimes. We can see no reason to re-open again the debate on issues so recently considered.

Date 29 November 2011