Corporate Governance in the UK: Views from Institutional Investors

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Institutional investors

- Definition
  - Public/private pension funds, occupational pension funds , mutual funds, insurance companies, investment trust and other financial institutions (O'Barr and Conley, 1992, Myners, 2001)
- Role:
  - As owners - safeguard their investment (feduciary responsibility)
  - Business relationship with the firm (Finkelstein, 1992, Heard and Sherman, 1987)

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Relevance

- In the UK individual ownership has decreased from 54% in 1963 to 10.2% in 2008 (£117.8 billion)
- Whilst institutional investment was 25.6 % in 2006, 29.9% in 2008 (£347,1 billion) (Office for National Statistics, 2010).

Influence on Corporate Governance

- Board composition and structure
  - Split chair/CEO
  - Board independence
- Committees and executive pay
  - Appropriate and skilled committees
  - Transparent pay and tied to performance
- Investor/company dialogue
  - Provides mutual understanding of objectives

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Methodology

- Structured interviews carried out in the Summer of 2008.
- Questions focus on three themes: thirteen prime questions
- Sample: 8 institutional investors
  - 3 investment trust companies,
  - 2 asset management companies,
  - 2 pension fund companies and
  - 1 insurance company (non had business relationships with investor companies)

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What investors said: Board composition

"We like to see a group separate the roles of chairman and CEO, have committees for remuneration, nomination and audit, have a substantial percentage of its board as non-execs, have a diverse board of directors, including women, have an ethics committee, and report at least annually on its [Board/ Corporate Governance] practices.".

"We will normally vote against the election of a director holding both positions unless a satisfactory explanation as to why these roles are combined"

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What investors said: Committees and executive pay

- *"Expect standard committees which should have appropriate skilled directors"*
- *"It aligns the interests of directors and shareholders"*
- *"It is right that the board should report each year in some detail its remuneration policy and how that policy was implemented over the year. We have for some time advocated that companies put the board's remuneration report to shareholders for a vote at the annual general meeting"*
- *"If a company is performing well and value is returned to the investor, then a director's remuneration is justified in being higher. If not, then a director's pay should reflect this".*

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What investors said: Investor/company dialogue

- *"we use a range of communication methods when engaging with companies that we hold. There is no fixed cycle."*
- *"communicate through constructive dialogue", "engage directly"* or "*keep regular communication with the management of the company"*.
- *"We visit every company (several times) before investing in it on behalf of our shareholders. We complete a corporate governance check on companies as part of our quality / value rating of companies; every company in which we invest must pass this first hurdle of financial strength, of which corporate governance is a part."*

What investors said: Investor/company dialogue

- *"There aren't that many issues that come up requiring public criticism. Also, we usually hold fairly large positions in investee companies, so we see our role as trying to change an organization from the inside, rather than trying to embarrass / criticize it from the outside."*

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