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Supplementary Response to Consultation on "Effective Company Stewardship" Adoption of Nomination Committees

Dear Mr Haddrill,

Further to our previous submission on the above topic, on behalf of the board of ShareSoc I would like to make some further comments which are given below.

You specifically recommend "there should be greater investor involvement in the process by which auditors are appointed". It has come to our attention that Tomorrow's Company published a report entitled "Tomorrow's Corporate Governance" last year (available from www.forceforgood.com/Uploaded_Content/tool/243201011485875.pdf). This covered the current arrangements in Sweden whereby nomination committees are used to recommend the appointment of auditors, the appointment of directors and the remuneration of the latter. These committees are formed from shareholders and prepare recommendations for General Meetings who make the final decisions on those matters (although as in the UK, these decisions are rarely challenged at the AGM). But the key point is that it is the shareholders who produce the recommendations to be voted upon rather than the managers of the company or the board of directors as in the current UK system. The Chairman of the board of directors of the company usually has a seat on the nomination committee but otherwise it comprises shareholder representatives.

This system appears to have been very effective in Sweden and has enabled much closer "engagement" of institutional shareholders with companies. In addition it also provides for some representation from individual shareholders who often have a seat on the Nomination Committee. It would appear to provide for a more consultative approach to the affairs of a company, and avoids the dominance of Chairmen or Chief Executives that takes place in UK companies. This tends to arise because other directors are dependent for their appointment and remuneration on the board of directors or its Chairman and it tends to encourage the development of "old boy networks" to the disadvantage of new blood (for example, the problem of the under representation of women on UK boards).

ShareSoc strongly recommends the universal adoption of shareholder lead Nomination Committees with the requirement that at least one proposed member is from a recognized private shareholder association. This would ensure that the large total of private shareholders in collective holdings held directly and indirectly via broker nominee accounts and other collective investment vehicles are adequately represented.

If a nomination committee was used to recommend the appointed of auditors, the shareholders would then be able to avoid the current conflicts of interest where auditors often provide other major services to a company, and where auditors see themselves as solely accountable to the board of directors of the company who appoint them.

The advantage of involving private shareholders in nomination committees would be:

- 1) Private shareholders are generally long term loyal shareholders with the best interest in the company's long term success. Their interest is aligned.
- 2) Having a representative from a recognized Private Shareholder Association would enable the natural selection of suitable candidates over time and those organizations can select and train suitable candidates like the other institutional holders who might be represented on a nomination committee.
- 3) Private shareholders also by the nature of their smaller shareholdings are likely to be less inhibited than institutional employees and hence may be willing to say what is avoided by such employees. This might be a valuable contribution to the committee's function.
- 4) Private shareholders are the ultimate beneficiary of the many intermediaries managing their investments on their behalf and would collectively easily exceed more than a 5% stake in all listed companies. Private shareholders thus have a greater right for representation than most if not all institutional investors.

We would certainly recommend you read the report mentioned above which not just explains the structure of the system but gives some insights into how it operates in practice. It appears to have re-invigorated the stewardship of Swedish public companies and the role of the General Meeting, and although there are some differences in the Swedish corporate structure to that of UK public companies, the shareholding structure is not greatly different. The key is surely to improve the accountability of companies to their shareholders and that is what the Swedish system appears to have achieved.

Yours sincerely

Roger W. Lawson
Chairman

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