Opinion

COMPANY HIERARCHIES

Most boards fail to walk the talk of increased shareholder agency

The promise of a new era in corporate governance brought by Companies Act has not come to fruition, write Audrey Elster and Kathleen Satchwell

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Illustration: KAREN MOOLMAN

There was a lot of excited chatter about a new era of shareholder activism when the Companies Act of 2008 came into effect in 2011. It wasn't just the substantial new appraisal rights shareholders were given and the improved derivative action remedy. There was also the enhanced ability of shareholders to call a meeting, as well as the seeming ease with which they could now propose resolutions to be considered at a shareholders meeting.

The excitement, which led to nervous tension in boardrooms, was reminiscent of the excitement that followed the launch of the King Report on Corporate Governance in 1994. That report was the first "establishment-aligned" document to formally highlight the important role shareholders had to play in effective governance of companies. However, while it sought to encourage more active engagement, the report made little distinction between shareholders and other stakeholders. And, despite the nod to stakeholders, it seemed intent on stressing the legal supremacy of the board, frequently referring to the need for a proper balance "between freedom to manage, accountability and the interests of the different stakeholders".

Twenty three years later the King 4 code has enhanced the distinct role and responsibility of shareholders. "The board should oversee that the company encourages proactive engagement with shareholders, including engagement at the AGM of the company," said King 4. It also urged the board to ensure shareholders are equitably treated and that the interests of minority shareholders are adequately protected.

As could be expected, most of the shareholder-related focus was on institutional investors, which is perhaps why it is only institutional investors that are deemed to have responsibilities, as outlined in principle 17. "The governing body of an institutional investor organisation should ensure that responsible investment is practised by the organisation to promote the good governance and the creation of value by the companies in which it invests," says King 4.

A few years later and excitement has subsided and been replaced by a jaded cynicism. Though it is encouraging that at least a few resolutions at every AGM get the thumbs down from 20% or so of shareholders, it's difficult not to suspect rote voting based on advice from a third party. Evidence that little of substance has changed in shareholder engagement is that despite substantial AGM votes against remuneration policies, the level of subsequent engagement involves a mere 2%-3% of shareholders.

In essence the critical role of shareholder activism has been left in the hands of a few brave individuals forced to incur hefty costs to secure their rights as shareholders. The powerful institutional investors in which King 4 put so much faith are nowhere to be seen. Unsurprisingly, though they still have their lawyers on speed-dial, boards across SA relaxed once they realised it was business as usual.

It is easy to see why King 4 and company law initiatives have resulted in little more than the creation of an industry focused on ticking off an ever-growing ream of corporate governance rules and recommendations. Remarkably, for documents that are supposedly enlightened, the Companies Act and King 4 do nothing to reduce the hefty cost and complexities of enforcing shareholder rights.

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Boards have been able to hunker down behind the ostensibly powerful protection of "fiduciary duty". In large part they have been aided and abetted by institutional investors, whose interests are uncomfortably aligned with boards. These powerful players have become experts at ticking all the boxes and giving an impression of activism.

The need to look outside the establishment for real change is why the Raith Foundation decided to launch its own Investment Stewardship Plan in 2016. As Raith sees it, key to stewardship is responsible investment, which seeks to generate financial and sustainable value.

Responsible investment aims to promote the long-term success of companies in such a way that the ultimate providers of capital also prosper. Stewardship entails monitoring, engaging and intervening — if appropriate — on matters that may affect long-term value, and on the companies' activities in social, environmental and other governance areas.

As part of its stewardship plan, Raith has engaged with a number of powerful listed companies. The experience has provided a salutary lesson on just how difficult it is to engage with vested interests that regard any engagement as a challenge to their authority.

It has also been disappointing to realise that, despite all the talk about shareholder activism, any engagement with a company requires a substantial commitment from the shareholder; the sort of commitment that is well beyond what's available to non-institutional shareholders.

While the overriding response to our overtures has generally been defensive, Raith has identified some subtle distinctions in the detail of that response. They range from encouraging to overwhelmingly discouraging.

The more sophisticated companies, which have well-resourced investor relations departments, encourage hopes of worthwhile engagement. An ostensibly well-meaning individual will be tasked with ensuring that every one of your communications is acknowledged, and no matter how long it takes a response will be provided; meetings will be set up with key decision makers; over the course of weeks, possibly months, discussions are held, all in a seeming effort to wear you down.

Beyond interminable polite meetings nothing happens. There is nothing as decisive as a formal rejection of Raith's suggestions, as this would run the risk of prompting further action. This is shareholder engagement by attrition.

Then there are those less sophisticated companies that tend to use their investor relations departments for damage control. Their CEOs and boards are outrageously ignorant of 21st-century governance obligations and are firmly trapped in a mid-20th-century mind-set, which allows little or no scope for any form of engagement with shareholders beyond the release of results.

The more enlightened of these will acknowledge communications and, if necessary, apologise for inappropriate actions before repeating those very same actions. The less enlightened will barely acknowledge communication from shareholders.

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On disturbingly rare occasions we have come across companies that are intent not only on listening to the concerns of their owners but on acting upon those concerns.

We have recently been encouraged by our initial engagements with Standard Bank, which give the impression that it is prepared to listen to our concerns. However, it has yet to indicate it is willing to act on those concerns.

In stark contrast, our engagement with Naspers, while initially encouraging, quickly became disappointingly hostile. This is of particular concern given that Naspers is SA's most valuable listed company and accounts for about 20% of the JSE top 40 index. As with all Naspers shareholders, Raith has done extremely well out of the group's dramatic share-price performance over the past 13 years, but our attempts to engage with the group have created the disturbing impression that Naspers believes it is too rich and powerful to have to account for its actions.

Raith believes the governance matters raised by the disclosure of payments from Naspers subsidiary MultiChoice to the Gupta-owned television station ANN7 warranted shareholder engagement. We [illegible] persuaded by the findings of an internal review that concluded there was no evidence of corruption or other illegal activity by

MultiChoice. But far from attempting to allay our concerns, Naspers refused to give us sight of the internal review, forcing us to launch an action in terms of the Promotion of Access to Information Act. As that application has been rejected we are now considering what options we have to give effect to our rights as shareholders.

It is important to point out that at all times in its engagements Raith understands and is supportive of the fact that directors have fiduciary duties to their company. These duties represent the cornerstone of a system of governance designed for large companies where the ownership (the shareholders) is separated from control (the board). We also support the greater powers given to directors by the new Companies Act.

We have no desire to challenge these critical duties and powers, but we are concerned by the manner in which directors are trotting them out as reason for not engaging with their shareholders. The disturbing implication of this sort of defensive attitude is that shareholders are deprived of any scope to exercise their responsibility to influence behavioural changes that lead to better stewardship.

They are left with the totally unacceptable alternative of selling their shares.

It is remarkable that South Africans are so intolerant (appropriately) of underperforming politicians, and yet so seemingly tolerant of underperforming boards.

• *Elster and Satchwell are with the Raith Foundation.*