

Engagement With Shareholders By Independent Directors

By Mike Gray
Independent Director



Introduction

Independent directors of listed entities in Singapore sometimes tend to stereotype a shareholder as someone, often elderly, who turns up to the AGM with the main purpose of partaking in the free lunch after the meeting. The independent director will normally mill around with the shareholders after the meeting and share pleasantries over a cup of tea or coffee. At the worst a shareholder may actually ask a question at the AGM. The independent director need not fear as management will have usually guessed the main questions and will have provided a crib sheet with the agreed answers, which management or the chairman will answer.

The situation has to some extent been cosy over the years, with directors not viewing shareholder engagement as part of their job and shareholders not expressing much interest in speaking to directors. However, shareholder activism is on the rise in Singapore. Recent activity includes the removal of a chairman at WBL Group, rejection of the re-appointment of board members

at an AGM of Grand Banks Yachts Ltd, the calling of an EGM by hedge funds to put three of their nominees on the board of Macquarie International Infrastructure Fund and the collapse of the share price of Olam International Ltd on a negative report by a shareholder - Muddy Waters. There are a number of other instances. In many of these cases the moves by shareholders came as a

surprise as management and the board were not fully aware of the shareholder grouses or how to deal with them. This could be an indication a lack of adequate shareholder engagement.

The writing of this article and a shift in my own position on shareholder engagement from that of limited involvement, results from me being personally caught in some situations

similar to those set out in the paragraph above. This article will look at shareholder engagement from the perspective of independent directors rather than that of management or executive directors.

What Is Shareholder Engagement?

Shareholder engagement is the forum or means by which shareholders can give their views to the Board and the Board can communicate directly to the shareholders.

Some guidance as to shareholder engagement can be found in the Singapore Code of Corporate Governance (the “Code”) which states that the Board needs to “identify the key stakeholder groups and recognise that their perceptions affect the company’s reputation”. In addition the Chairman should “ensure effective communication with shareholders”.

The Code, in the section on “Communication with Shareholders” sets the principle that “Companies should actively engage their shareholders and put in place an investor relations policy to promote regular, effective and fair communication with shareholders”.

This is further expanded in the Code under the Guidelines, which state that:

- “Companies should devise an effective investor relations policy to regularly convey pertinent information to shareholders. In disclosing information companies should be as descriptive, detailed and forthcoming as possible, and avoid boilerplate disclosures.
- The Board should establish and maintain regular dialogue with shareholders, to gather views or inputs, and address shareholders’ concerns.
- The Board should state in the company’s Annual Report the steps it has taken to solicit and understand the

views of the shareholders e.g. through analyst briefings, investor road shows or Investors’ Day briefings”.

In summary the board has a fiduciary duty to take into account the shareholder interests and concerns. To this end, directors have to understand the shareholders’ views on the company, its governance and its operations.

Why Do It?

Whether one likes it or not shareholder engagement has become important as shareholders, particularly if they gang up together, may end up voting down resolutions, calling EGMs, removing directors and putting their nominees on the board etc. In this age of high technology it is much easier for shareholders to disseminate their views publicly and join together with other shareholders into a lobby group. Also dissident shareholders can go viral with their grouses resulting in pressure on both the share price and on management.

What is important to note that such aggressive action may be taken by shareholders due to frustration rather than for any apparent concrete reasons. Shareholders are continuously looking towards better governance, improved transparency and risk management by the board. In addition shareholders may have views on how the company should be run and want their views heard. The danger from aggressive shareholders becomes more of an issue if the entity is exhibiting poor financial performance and shareholders are unable to get comfort that the board is tackling the issues properly. The formal written disclosures, required by the Companies Act and the Listing Manual, may not be enough to satisfy these shareholders.

Finally the Code of Corporate Governance does require that the boards of listed entities have an adequate shareholder engagement programme as mentioned above.

Why Should It Concern Independent Directors?

In the past it has normally been management that has been the source of communications between the listed entity and the shareholders. However, shareholders are now often expecting direct access to boards, due to an increase in expectations of the board with the enhancement of the corporate governance process. It may be also because shareholders are not sure whether their views are being passed to the Board, or whether management are accurately disseminating board policies.

Traditionally the Chairman of the Board has been the main contact but more frequently the independent directors are being drawn into discussion with shareholders. Typically this may happen if the chairman is executive and not independent or if the number of shareholders to be contacted is so large that the task needs to be shared. In some cases it may be that the chairman is the problem as far as the shareholders are concerned and they do not want to meet with the chairman.

Benefits Of Shareholder Engagement

Boards typically are worried about shareholder engagement as they fear that the shareholders may be stirring up trouble. This may not always be the case. Institutional shareholders could have extensive exposure to business strategies in a sector and may be able to provide useful advice to the board. In addition an external view on the company’s performance may help fine tune strategies and provide an early warning signal of any issues. Finally, through better engagement, board members will be able to better understand the views of shareholders with respect to the company.

A further benefit of shareholder engagement is that it can increase

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shareholder goodwill and trust. Shareholders, who have an interactive relationship with the board, will be more likely to support the board when it comes to the vote and are less likely to call EGMs, which are often initiated to establish dialogue with boards that ignore them. Furthermore dialogue with shareholders may bring up issues that they may have early and before they become a rallying point, particularly if such issues arise out of misunderstandings between them and the board.

Issues With Shareholder Engagement

One of the most difficult issues concerning shareholder engagement by independent directors is making sure that one avoids selective disclosure of sensitive information. The SGX listing rules, Paragraph 7 of Appendix 7.1, provides that information must not be divulged to any person outside the listed entity & its advisers, in such a way as to place such person in a privileged dealing position and Paragraph 23 of Appendix 7.1 provides further that under no circumstances should disclosure of material information be made on an

individual or selective basis to analysts, stockholders or other persons unless such information has been previously fully disclosed and disseminated to the public.

Before letting independent directors loose on the shareholders, it is important that the company's disclosure policy should be communicated to them together with guidelines on what constitutes material information. In particular discussions with shareholders should avoid internal financial projections, strategic plans, significant undisclosed developments, specific business opportunities, and potential dividend policies or share buy backs. In fact anything that could be expected to affect the market price of the shares.

The role of management versus the board in shareholder engagement needs to be clearly defined and communicated to shareholders. In general management normally will have driven shareholder communication, through the CEO, with the board overseeing the process. If the board is to be involved, shareholders need to be informed of this fact as they may be confused as to whom to contact. As regards the position of management, they may feel a threat that

board members are discussing major issues behind their backs and side lining them. To this end communication with management must be maintained at all stages. Most importantly, the same and not conflicting messages need to be passed to shareholders by both management and the board. Far too often, in practice, either management or a board member tends to speak out of place in a one to one meeting with shareholders.

Analyse Your Shareholder Base

The extent of shareholder engagement will depend very much on the shareholder base of the entity. Shareholder groups may include:

- **Institutional investors** – tend to rank amongst the larger investors. They may include insurance companies, pension funds, mutual funds etc. They are accountable to the beneficiaries whose funds they manage and can exert influence in the management of companies because of their large voting rights. Sometimes they will be forced to vote one way or another because of a mandate.
- **Activist shareholders** – are often hedge funds. These are the most dangerous of the shareholder groups for boards and need to be watched carefully. The objective of a hedge fund is normally to make a quick profit and they may have a very short term view of the investment. They often look for entities with a weak performance and can often put pressure on management to act in accordance with their wishes by threatening proxy contests if they do not get their own way.
- **Retail investors** – tend to be small by levels of investment but may be vociferous at AGMS.
- **Family shareholders** – Some listed entities are still controlled by family shareholders. Boards in this type of

entity are always subject to the thread of removal should they fall foul of the family.

- **Hidden shareholders** – some shareholders hide behind various overseas corporate entities and it may be impossible to contact beneficial shareholder. These are the most difficult to deal with as you do not know who they are or why they may be voting a particular way on a resolution.

Shareholders do not consist of a homogeneous group. The investor time frames, size, resources, personal interests may differ. Some may be passive investors and others may be activists. To this end it is important to know who your major shareholders are and what their principal reasons are for investing in the company.

Once you know your shareholders you can set the priority as to which shareholders you need to engage with and the extent of such engagement.

The Engagement Meeting With Shareholders

There are many different ways, in addition to statutory disclosures and discussions at general meetings, that the board may choose to engage with shareholders. These include passive feedback, shareholder surveys, websites, blogs, conference call dial in etc. For the purpose of this paper I will only consider the one to one meeting between the independent director and shareholder as most of the other methods will be carried out by management or consultants.

Prior to any meeting with a shareholder, the director should develop an agenda and collect the relevant information. Preferably find out in advance what topics the shareholder wants to cover. There is nothing worse than not being able to answer a question and fumble your way through the meeting. However, also be mindful that you must not disclose significant information that is not available to other shareholders.

Preferably directors should aim to meet the shareholder jointly with at least one member of senior management. If a shareholder insists on a one on one session with the director for any particular issue, the member of management can be excused for that item. In any event if management is not attending the meeting the director should aim to be accompanied by another director or legal counsel, as witness to the discussion so as to avoid any potential misunderstandings.

If possible find an environment that is conducive so that the discussion can be as friendly and relaxed as possible. For major shareholders, discussion over a meal can be good way to break the ice. Personal contact rather than written is important. At the very minimum the director should call the shareholder by phone or such other electronic means that may be available such as “Skype”. Once a good relationship has been established it is so much easier to deal with the issues.

During the meeting, try to listen to the shareholder rather than becoming defensive. If there are grievances, tell the shareholder that you will look into

them. If the shareholder has ideas tell him that you will consider. Do not give decisions on matters raised unless they have been cleared prior to the meeting by the board/ management. It is also preferable not volunteer too much information unless questioned, as you may be trapped into mentioning issues that you may prefer not to disclose.

It is possible to turn around an aggressive shareholder group. Listen to their issues. Often they can be overcome one way or another. For instance is the shareholder has names for suggested board members, do not turn them down out right, but put them into the system with any board nominees. Preferably employ an external consultant to carry out the search so as the whole process can be seen to be independent of the board and the shareholders.

After the meeting make sure that you debrief both management and the board of the items discussed with the shareholder. With respect to the shareholder, it is important that contact is maintained on a continuing basis even though the issues may have been defused.

Conclusion

As regards shareholder engagement by directors there is no one size that fits all solution. Every company is different, shareholder bases are different and the issues are different. Some entities may require minimal involvement by independent directors others significant involvement. Directors need to identify clearly situations where shareholder engagement is necessary if they wish to avoid nasty corporate surprises that may hit them unaware. ■

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