



Investment Commentary by Roger Nightingale

Do the right thing: it will gratify some,
and astonish others.

Mark Twain, more the latter than the former, of course.

12th February 2010

Cadbury was voted into oblivion by a bunch of people who were not owners!

After the votes had been counted, it was established that those in favour of Cadbury's sale to Kraft outnumbered those opposed to it. The disposal duly went ahead. Was that a famous victory for democracy or an infamous abuse of governance? Opinions vary.

Is the Law being applied sensibly?

The key issue is whether those who voted were entitled to do so. The Law is ambivalent; it says that "owners" must be responsible for disposals, but doesn't always make it clear who the owners are. It doesn't say, for instance, whether shares "held" by a financial institution are also "owned" by it.

It wouldn't happen to a Landlord!

In other areas, there is no ambiguity; no confusion between principal and agent. If a man were to own a piece of land, but give its management to a steward, the latter would have no right to dispose of it without reference to the former. A prospective buyer might initially approach the agent, but the decision would be made subsequently by the principal—the beneficial owner.

Why are the beneficial owners of a company so pusillanimous?

Why should equity-based transactions be different? Aren't the Cadbury shares held in a Unit Trust beneficially owned by Unit Holders? Why then were the latter not consulted? Why were their rights usurped by managers?

It's habit not logic.

It's a function of Trust Law, say defenders of the status quo. They claim that the Unit Holder is the equivalent of the twelve year-old school girl who, though she will later become the beneficiary, is currently too young and inexperienced to make her own decisions. Her interests are protected by a Trust.

Regular abuse becomes gradually acceptable.

Perhaps so. But the parallel with Unit Holders is patently absurd. The latter are typically older and wiser than the gun-slinging fund managers who administer shares. Owners need protection, not from the impetuosity of their own decisions, but from that of their managers!

It was much the same with Union Bosses in earlier decades.

A second line of defence is that the proposal to refer issues of governance back to beneficial owners would be impractical. Hmph! That was what was said when it was proposed that Union Bosses not make strike decisions themselves, but seek the opinion of their members. The parallel is apt. Before the rules were changed, General Secretaries used to appropriate the voting rights of their worker-members; today, it is Chief Executives of Insurance Companies and Pension Funds who do the same to shareholders.

But the rules there were eventually changed.

There was another culprit involved in the Cadburys debacle; another agent that had presumed the powers of a principal. It was the Board. Why did it concede defeat at the outset? Why did the Chairman and Finance Director quibble only about the price of submission? Why hadn't they devoted their energies to improving the on-going returns they earned for shareholders? What were the terms of their severance package?

Thatcher disciplined the Unions. When cometh such another?

The Law needs to be reviewed. It's not only the social environment that's broken; it's the financial one as well. Cameron and Osborne must be prepared to tackle delinquency, not just in schools but also in board rooms, not just on the streets but in fund management houses as well. Will they do so? Don't hold your breath.

The facts and opinions contained within this newsletter have been provided by Roger Nightingale; Buckles Investment Services do not take any responsibility for the contents.

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